ECONOMY: Falling Oil Benefits Global Growth

A REVERSAL OF FORTUNE
The beginning of 2015 has been marked by an environment of increased volatility within the global investment markets. Commodities continue to suffer, rates continue to fall, and developed international equities are outperforming the U.S.

Q4 GDP
The first estimate of fourth-quarter U.S. gross domestic product (GDP) rose 2.6%. Consumer spending increased sharply, up 4.3% quarter-over-quarter, the largest quarterly and annual gain since 2006, on the back of increased confidence, a strengthening labor market, and lower gas prices.

EYE ON THE FED
The Federal Reserve is expected to begin normalizing monetary policy in the second half of the year. However, shifting views on the Fed’s timing outlook, economic developments outside the U.S., and geopolitical tensions are likely to keep financial market volatility at elevated levels.

INFLATION DATA WEAK
Core inflation, which excludes food and energy, rose 1.6% over the 12 months ending in December. The sharp drop in oil and gasoline may feed through indirectly to lower core inflation in the near term. Fed officials view the drop in energy prices as “transitory,” but low inflation may delay the initial rate hike.

CONSUMER CONFIDENCE HIGHEST SINCE 2007
The Conference Board Consumer Confidence Index®, which had increased in December, rose sharply in January. “Consumer confidence rose sharply in January, and is now at its highest level since August 2007 (Index, 105.6). A more positive assessment of current business and labor market conditions contributed to the improvement in consumers’ view of the present situation. Consumers also expressed a considerably higher degree of optimism regarding the short-term outlook for the economy and labor market, as well as their earnings.”

CURRENCY WARS
The Swiss Franc posted a sharp rise against the Euro as a result of the Swiss National Bank’s abandonment of the currency cap to the Euro. Additionally, the Euro also fell sharply as a result of the ECB’s initiation of bond purchase stimulus measures, as well as the election victory of an anti-austerity Syriza party in Greece.

IMF DOWNGRADES GROWTH OUTLOOK
Typically, the IMF updates its World Economic Outlook twice a year—April and October. When global economic conditions change substantially, it will provide an interim update. The oil shock and its effects on the global economy warranted such an action. The IMF cut its Global GDP forecast for 2015 and 2016 to 3.5 percent and 3.7 percent, respectively, citing lower oil prices and “a reassessment of prospects in China, Russia, the euro area and Japan.” This represents a downward revision of at least 0.3% for each year.

SETUP FOR EUROZONE RECOVERY?
Three powerful forces should boost Euro area growth in 2015. The currency has plummeted nearly 20% versus the dollar, benefitting exporters. Second, the crash in oil prices is a boost for Euro area consumers and businesses. Third, the ECB’s implementation of “quantitative easing” should benefit the region as credit becomes more readily available.

EUROZONE RISKS
The region continues to fight deflationary pressures (falling prices), which has been exacerbated by falling oil prices. Additionally, the region is watching the political risk associated with the new Syriza led government in Greece. Thus far, the new government has balked at some of the mandates from Greece’s 2008 bailout. The risk of default or an exit from the currency union has risen.
GLOBAL EQUITIES: Volatility Returns

A Volatile Start to the Year
The beginning of 2015 was marked by significantly higher volatility in the equity markets. Of the 20 trading days in January, the closing price of S&P 500 changed by greater than 1% eight times. On an intraday basis it was much worse. On 18 of the 20 trading days, the intraday high and low on S&P 500 was greater than 1%. The S&P 500 Volatility Index (VIX), often referred to as the “fear index,” spiked above 20 on three separate occasions in January.

The Earnings Report
S&P 500 fourth quarter earnings have been relatively strong thus far. With nearly 70% of S&P 500 companies having reported, 81% have beaten or met earnings expectations. The technology sector has been notably strong. With nearly 82% of the companies in the sector having reported, 86% have beaten expectations.

The January Barometer
There is an old stock market adage saying, “so goes January, so goes the year.” One often followed metric is the January Barometer, devised by Yale Hirsch in 1972 for The Stock Traders’ Almanac. The January Barometer has registered eight major errors since 1950 for an 87.7% accuracy ratio. For 2015 the January Barometer indicator is negative for the second year in a row and five of the last eight years. Since 2000 January has been down 7 of the last 15 years with an average loss of 1.2% on the S&P 500. Interestingly though, five of the indicators’ eight major errors have occurred in this 15-year timeframe.

Around the Globe
Global equity diversification benefitted investors in January, as much of the developed and emerging world outperformed the U.S. In developed Europe, the equity markets of Sweden, Denmark and Germany all posted strong returns. While returns for the region were flat, it outperformed the U.S. by 3% on a relative basis. The MSCI Emerging Markets index was up 0.60% to start the year, buoyed by positive returns in India, Egypt, South Africa and China.
**FIXED INCOME: Treasuries Rally**

**TREASURIES RALLY**
Intermediate- and long-term U.S. Treasury debt rallied strongly, driving the yield on the 30-year Treasury to record lows. The benchmark 10-year Treasury note's yield decreased by 49 basis points over the course of the month to finish at 1.68%, its lowest level since May 2013. The Barclays U.S. Aggregate Bond Index returned 2.1%, while the Barclays U.S. Treasury and U.S. TIPS indices returned 2.6% and 3.2% respectively.

**ALPHABET SOUP – ECB QE**
The extremely low yields on other high-quality government bonds helped support U.S. Treasuries by making their yields attractive in comparison. The 10-year German Bund yielded only 0.30% at months end, after the European Central Bank (ECB) announced its long anticipated quantitative easing program (QE). The ECB will expand its asset purchases in March to include sovereign bonds, and said that it will buy €60 billion (about $67 billion) per month of bonds through at least September 2016 to inject a larger-than-expected total of more than €1 trillion into the eurozone economy.

**HIGH YIELD RECOVERS**
Unlike the last couple of months of 2014, when plummeting oil prices dragged down the high yield bond market, noninvestment-grade bonds returned 0.70% in January. Low energy and commodities prices continued to weigh on the sector, but a slowdown in new issuance from last year should provide some support.
CTAs Continue to Shine
Hedge funds posted mixed performance to start off 2015. While the HFRX Global Composite fell 0.30%, the HFRX Macro and Systematic Diversified CTA (Commodity Trading Advisor) indices generated strong relative performance. The HFRX Macro Index posted a gain of 2% for January, its best monthly performance since November 2009 and the 9th consecutive monthly gain. Positive contributions came from systematic trend-following managers and discretionary currency funds. The HFRX Systematic Diversified CTA Index gained 3.4% for January and benefitted from long Swiss Franc and global fixed income positions, and short oil and Euro positions.

Lower Rig Count Won’t Impact Production
U.S. drillers cut rigs targeting oil by a record 435 to 1,140 thus far this year, according to Baker Hughes Inc. That’s the lowest total since December 2011 as explorers slow efforts in the Permian Basin in Texas and North Dakota’s Bakken formation. However, U.S. production will increase by 7.8 percent to 9.3 million barrels a day this year, the fastest pace since 1972, according to the Energy Information Administration. Goldman Sachs noted that producers are closing rigs with the least-efficient output first, meaning more drilling has to stop to temper the increase in supplies.

REIT Momentum Continues
REITs started 2015 on solid ground, as continued low interest rates and promising fundamentals helped the sector outperform the broader market in January. While the broader market was impacted by jitters concerning oil prices, the dollar and Europe’s economy, interest rates fell and the growth in the underlying economy signaled that there should be solid demand for real estate. Almost all REIT sectors performed well in January. Gains were led by the self-storage sector, which rose 9.6%, while Health Care REITs trailed slightly, up 9.3%