

Macro Talking Points

Fixed Income Insights

Week of 5 February 2024

Author



Benoit Anne
Managing Director
Investment Solutions Group

In brief

- **The macro backdrop remains robust, with evidence for an imminent recession looking weaker.**
- **Investor cash allocations are coming down.**
- **Global fixed income is off to a sluggish start performance-wise, but the outlook looks brighter.**

Where is my hard landing? Wherever we look, it is getting harder and harder to find evidence of an imminent recession, at least in the United States. To say the least, nonfarm payrolls (NFP) running to +300,000 are not consistent with recession risks.¹ The average gain in payrolls over the past three months stands at 289,000. Let's contrast that with history. For most of the recessions since the 1960s, the NFP average for the three months immediately preceding the beginning of a recession has typically been well below 100,000 before declining once the recession started. So, it's fair to say that NFP doesn't currently signal a high risk of recession. What about productivity, which surprised to the upside for Q4? Same story there. It would be highly unusual if productivity accelerated in advance of a recession. Typically, prior to a downturn, productivity tends to slow markedly or even turn negative. More good news comes from capex expectations. We have updated our capex expectations indicator and, overall, there are no signs that companies in the US intend to cut capital spending. Finally, all the business surveys, be it the ISM or PMI, seem to be ticking up. In fact, the recent ISM new orders number, considered to be one of the most leading of leading indicators, recovered sharply in January. This all seems to suggest that the soft-landing scenario is gaining traction. That's good news for risky assets and fixed income spread products, from a macro perspective.

Cash is no longer king. Cash allocations had been on the high side, reflecting persistent investor caution, but now seem to be declining. To be clear, the data can be challenging. We use two main sources for our cash allocation tracking. The first is produced by the American Association of Individual Investors (AAII) which is geared towards the retail business.² The AAII data show that cash allocation is now well off its recent peak and has converged towards its 10-year average. The second data source we keep an eye on is the BofA Global Fund Manager Survey data which looks at asset manager behavior.³ Again, cash allocations are well off their recent highs, although they still seem elevated by historical standards. The key message here is that cash allocations are going in the right direction — meaning lower — but there may be more room to go as we believe that the macro environment has turned more supportive of risk taking. At the same time, all these central bank rate cuts in the pipeline are inevitably going to undermine cash return expectations in the period ahead. In my view, it's about time investors moved away from cash and bought riskier assets.

Not so happy new year so far, but it will likely get better. It has been a fairly rough start to the year for global fixed income, in contrast to 2023's spectacular close. Virtually all sub-asset classes have suffered negative performance year to date. The Global Agg has printed a loss of 1.97% so far in 2024, the worst performance among the fixed income sub-asset classes we are monitoring.⁴ EM local debt and global credit have also registered sizeable negative returns. The key driver of this poor start is clear: Market rates have risen by more than 20 basis points in the US 10yr segment, mainly reflecting pushback on the part of the US Federal Reserve. The good news is that the Fed cut pricing correction over the past week has now put us on a stronger footing with respect to monetary policy expectations, especially as the March rate cut has virtually been priced out. Listening to Fed Chair Jerome Powell, there is still a risk that even a May Fed rate cut might seem premature, but the May odds look solid to us. By May, the Fed would have had the opportunity to observe and analyze three monthly CPI and three core PCE price index releases. In other words, plenty of time, in our view, to gain more comfort with the appropriateness of rate cuts. Despite a sluggish start to the year, we believe that global fixed income remains very well positioned in 2024. The macro environment is robust and supportive of spread products, while rates are likely to benefit from the dovish central bank policy action. Altogether, this should help boost fixed income performance in the year ahead. For investors that have yet to increase their allocation to fixed income, this slow start provides an attractive entry point to do so. ▲

Endnotes

¹ Bloomberg, Bureau of Labor Statistics. US Employees on Nonfarm Payrolls Total MoM Net Change. As of January 2024.

² Bloomberg, American Association of Individual Investors. AAll Cash Allocation. Monthly, as of January 2024.

³ BofA, Global Fund Manager Survey. Data as of December 2023.

⁴ Bloomberg. Bloomberg Global Aggregate Index, data as of 2 February 2024.

Source: Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively “Bloomberg”). Bloomberg or Bloomberg’s licensors own all proprietary rights in the Bloomberg Indices. Bloomberg neither approves or endorses this material or guarantees the accuracy or completeness of any information herein, or makes any warranty, express or implied, as to the results to be obtained therefrom and, to the maximum extent allowed by law, neither shall have any liability or responsibility for injury or damages arising in connection therewith.

The views expressed herein are those of the MFS Investment Solutions Group within the MFS distribution unit and may differ from those of MFS portfolio managers and research analysts. These views are subject to change at any time and should not be construed as the Advisor’s investment advice, as securities recommendations, or as an indication of trading intent on behalf of MFS.

Unless otherwise indicated, logos and product and service names are trademarks of MFS® and its affiliates and may be registered in certain countries.

Distributed by: **U.S.** – MFS Institutional Advisors, Inc. (“MFSI”), MFS Investment Management and MFS Fund Distributors, Inc., Member SIPC; **Latin America** – MFS International Ltd.; **Canada** – MFS Investment Management Canada Limited. **Note to UK and Switzerland readers:** Issued in the UK and Switzerland by MFS International (U.K.) Limited (“MIL UK”), a private limited company registered in England and Wales with the company number 03062718, and authorised and regulated in the conduct of investment business by the UK Financial Conduct Authority. MIL UK, an indirect subsidiary of MFS®, has its registered office at One Carter Lane, London, EC4V 5ER. **Note to Europe (ex UK and Switzerland) readers:** Issued in Europe by MFS Investment Management (Lux) S.à r.l. (MFS Lux) – authorized under Luxembourg law as a management company for Funds domiciled in Luxembourg and which both provide products and investment services to institutional investors and is registered office is at S.a r.l. 4 Rue Albert Borschette, Luxembourg L-1246. Tel: 352 2826 12800. This material shall not be circulated or distributed to any person other than to professional investors (as permitted by local regulations) and should not be relied upon or distributed to persons where such reliance or distribution would be contrary to local regulation; **Singapore** – MFS International Singapore Pte. Ltd. (CRN 201228809M); **Australia/New Zealand** - MFS International Australia Pty Ltd (“MFS Australia”) (ABN 68 607 579 537) holds an Australian financial services licence number 485343. MFS Australia is regulated by the Australian Securities and Investments Commission.; **Hong Kong** - MFS International (Hong Kong) Limited (“MIL HK”), a private limited company licensed and regulated by the Hong Kong Securities and Futures Commission (the “SFC”). MIL HK is approved to engage in dealing in securities and asset management regulated activities and may provide certain investment services to “professional investors” as defined in the Securities and Futures Ordinance (“SFO”); **For Professional Investors in China** – MFS Financial Management Consulting (Shanghai) Co., Ltd. 2801-12, 28th Floor, 100 Century Avenue, Shanghai World Financial Center, Shanghai Pilot Free Trade Zone, 200120, China, a Chinese limited liability company registered to provide financial management consulting services.; **Japan** - MFS Investment Management K.K., is registered as a Financial Instruments Business Operator, Kanto Local Finance Bureau (FIBO) No.312, a member of the Investment Trust Association, Japan and the Japan Investment Advisers Association. As fees to be borne by investors vary depending upon circumstances such as products, services, investment period and market conditions, the total amount nor the calculation methods cannot be disclosed in advance. All investments involve risks, including market fluctuation and investors may lose the principal amount invested. Investors should obtain and read the prospectus and/or document set forth in Article 37-3 of Financial Instruments and Exchange Act carefully before making the investments; **Bahrain** - This document has not been approved by the Central Bank of Bahrain which takes no responsibility for its contents. No offer to the public will be made in the Kingdom of Bahrain and this document is intended to be read by the addressee only and must not be passed to, issued to, or shown to the public generally. The Central Bank of Bahrain assumes no responsibility for the accuracy and completeness of the statements and information contained in this document and expressly disclaims any liability whatsoever for any loss howsoever arising from reliance upon the whole or any part of the contents of this document. The Board of Directors and the management of the issuer accepts responsibility for the information contained in this document. To the best of the knowledge and belief of the board of directors and the management, who have all taken all reasonable care to ensure that such is the case, the information contained in this document is in accordance with the facts and does not omit anything likely to affect the reliability of such information.; **Kuwait** - This document is not for general circulation to the public in Kuwait. The information has not been licensed for offering in Kuwait by the Kuwait Capital Markets Authority or any other relevant Kuwaiti government agency. No private or public offering of the information is being made in Kuwait, and no agreement relating to the information will be concluded in Kuwait. No marketing or solicitation or inducement activities are being used to offer or market the information in Kuwait.; **Oman** - For Residents of the Sultanate of Oman: The information contained in this document does not constitute a public offer of securities in the Sultanate of Oman as contemplated by the Commercial Companies Law of Oman (Royal Decree 4/74) or the Capital Market Law of Oman (Royal Decree 80/98). This information is being circulated on a limited basis only to corporate entities that fall within the description of sophisticated investors (Article 139 of the Executive Regulations of the Capital Market Law). The recipient acknowledges that they are a sophisticated investor who has experience in business and financial matters and is capable of evaluating the merits and risks on an investment.; **South Africa** - This document has not been approved by the Financial Services Board and neither MFS International (U.K.) Limited nor its funds are registered for public sale in South Africa.; **UAE** - This document, and the information contained herein, does not constitute, and is not intended to constitute, a public offer of securities in the United Arab Emirates and accordingly should not be construed as such. The information is only being offered to a limited number of exempt investors in the UAE who fall under one of the following categories of non-natural Qualified Investors: (1) an investor which is able to manage its investments on its own, namely: (a) the federal government, local governments, government entities and authorities or companies wholly-owned by any such entities; (b) international entities and organisations; or (c) a person licensed to carry out a commercial activity in the UAE, provided that investment is one of the objects of such person; or (2) an investor who is represented by an investment manager licensed by the SCA, (each a “non-natural Qualified Investor”). The information and data have not been approved by or licensed or registered with the UAE Central Bank, the Securities and Commodities Authority, the Dubai Financial Services Authority, the Financial Services Regulatory Authority or any other relevant licensing authorities or governmental agencies in the UAE (the “Authorities”). The Authorities assume no liability for any investment that the named addressee makes as a non-natural Qualified Investor diligence on the accuracy of the information relating to the securities. If you do not understand the contents of this document you should consult an authorised financial adviser.; **Saudi Arabia** - This document may not be distributed in the Kingdom except to such persons as are permitted under the Investment Funds Regulations issued by the Capital Market Authority. The Capital Market Authority does not make any representation as to the accuracy or completeness of this document, and expressly disclaims any liability whatsoever for any loss arising from, or incurred in reliance upon, any part of this document. Prospective purchasers of the securities offered hereby should conduct their own due diligence on the accuracy of the information relating to the securities. If you do not understand the contents of this document, you should consult an authorised financial adviser.; **Qatar** - This material/fund is only being offered to a limited number of investors who are willing and able to conduct an independent investigation of the risks involved in an investment in such material/fund. The material does not constitute an offer to the public and is for the use only of the named addressee and should not be given or shown to any other person (other than employees, agents or consultants in connection with the addressee’s consideration thereof). The fund has not been and will not be registered with the Qatar Central Bank or under any laws of the State of Qatar. No transaction will be concluded in your jurisdiction and any inquiries regarding the material/fund should be made to your contact outside Qatar.