

MIDYEAR OUTLOOK DEEP DIVE



JULY 23, 2019

AUTHORS

GLOBAL MACRO STRATEGY

Joe Seydl

Senior Market Economist

Jeff Greenberg

Senior Market Economist

Vinny Amaru

Market Economist

GLOBAL MARKET STRATEGY & ADVICE

Jake Manoukian

Global Market Strategist

GLOBAL EQUITY STRATEGY

Chris Baggini

Global Head of Equity Strategy

Nadia Lovell

U.S. Equity Strategist

Grace Peters

Europe Equity Strategist

Raymond Cheng

Asia Equity Strategist

GLOBAL FIXED INCOME, CURRENCY & COMMODITIES STRATEGY

Tom Kennedy

Global Fixed Income Strategist

Scott Schnipper

Head of Currencies, Commodities & Rates, U.S. & EMEA

The second half of 2019 will be defined by a delicate balancing act. Will the strength of the U.S. consumer be able to outweigh weakness in business spending? Will coordinated easing from central banks be enough to offset the uncertain outlook for trade policy? How should investors be positioned now that the expansion has become the longest in history?

In *Navigating a maturing cycle*, our midyear overview, we began to answer the questions above. We argued that investors should have a balanced, prudent allocation to risk in long-term portfolios while focusing on three key themes: investing in the secular growth trends of the future, harvesting yield and adding protection to help stay invested.

In this bulletin, market strategists from across J.P. Morgan's Capital Market Solutions teams take a deeper dive into these three key themes, laying out our macroeconomic rationale and identifying areas where, in our view, above-market returns may be achieved across asset classes.

THE MACROECONOMIC BACKDROP: Will U.S. consumer strength be enough to sustain the expansion?

Joe Seydl, Jeff Greenberg and Vinny Amaru

It's true for all our investment themes, but one in particular—**Finding growth in a low-growth world**—is closely tied to our macroeconomic outlook, discussed here in detail. We will explain our base, bull and bear-case scenarios along with when, how, and why growth may potentially slow. Before diving into the opportunities that remain for above-market returns, we detail the key trends and data points we're watching as the foundation of our outlook.

How material will the growth slowdown be?

U.S. economic growth over the past year has been pushed to 3% but that pace cannot be sustained, in our view. This recent period of growth was boosted by fiscal stimulus (tax cuts and government spending) as well as by large upswings in trade and inventory, as companies stockpiled ahead of impending tariff increases. None of these growth drivers are likely to be repeated. Past Fed hikes are still feeding through as well, and trade tensions add a layer of uncertainty.

INVESTMENT AND INSURANCE PRODUCTS ARE:

NOT FDIC INSURED • NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY

- NOT A DEPOSIT OR OTHER OBLIGATION OF, OR GUARANTEED BY, JPMORGAN CHASE BANK, N.A. OR ANY OF ITS AFFILIATES
- SUBJECT TO INVESTMENT RISKS, INCLUDING POSSIBLE LOSS OF THE PRINCIPAL AMOUNT INVESTED.

This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. Please read the Important Information section at the end of this article.

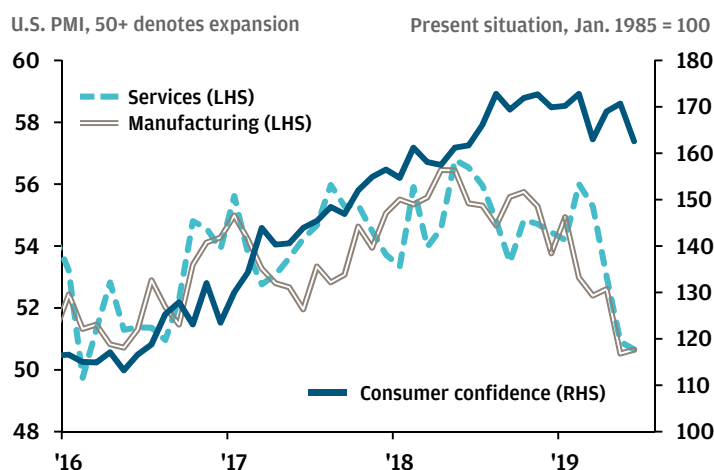
As the Federal Reserve (Fed) pivots to easing, the key question is whether a recent downturn in business sentiment will persist and send the U.S. labor market reeling and unemployment rising.

So far, the U.S. consumer is proving to be quite resilient

Initial jobless claims remain near all-time lows and recent solid retail sales reports have quashed lingering doubts about consumer strength. Despite corporate pessimism, the leading indicators of consumer spending show pronounced optimism (**EXHIBIT 1**). Consumer confidence remains robust and the employment component of the purchasing managers' indexes (PMIs) shows continuing hiring plans. Moreover, consumer balance sheets look healthy. In contrast to prior cycles, consumers are spending in line with their incomes and not overly relying overly on credit (**EXHIBIT 2**).

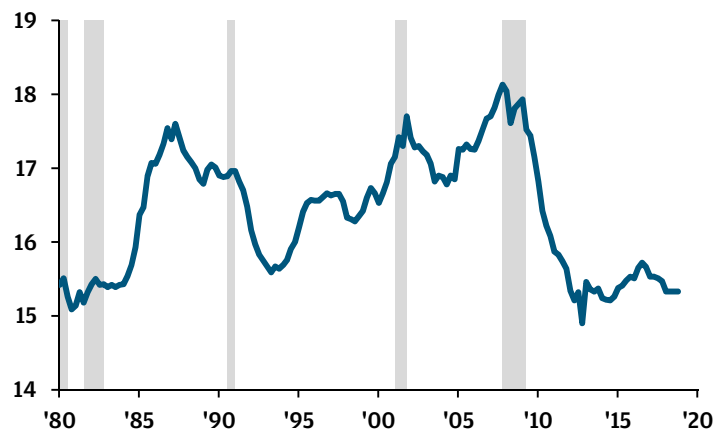
The consumer sector is still solid, but the business sector is slowing

EXHIBIT 1: U.S. BUSINESS CONDITIONS AND CONSUMER CONFIDENCE



Household balance sheets are healthier than in prior cycles

EXHIBIT 2: U.S. HOUSEHOLD FINANCIAL OBLIGATIONS AS A % OF INCOME



Our macro outlook: Downside risks remain elevated

Our base case is the U.S. economy slows toward trend real GDP growth of about 1.5%-2% (**EXHIBIT 3**). We do not see an imminent U.S. recession, as long as consumer strength, which is the backbone of the U.S. economy, continues. However, the uncertainties surrounding trade policy, we believe, skew the risk toward our bear case: a meaningful shock producing sub-1% growth and rising unemployment. We assign a 30% probability to our bear case occurring over the next six months.

EXHIBIT 3: BULL, BEAR & BASE CASES FOR U.S. ECONOMY

	Bear case (30% probability)	Base case (60% probability)	Bull case (10% probability)
Growth	Significant growth slowdown (GDP growth sub 1%)	Growth decelerates to trend (1.5%-2%)	Animal spirits rebound (GDP growth 3%+)
Labor Market	Labor market cracks (unemployment rising)	Unemployment rate remains below 4%	Unemployment rate falls close to 3% and wages rise faster than expected
Fed Policy	Fed cuts meaningfully (100bps or more)	Fed cuts rates twice (each by 25bps) with the first cut in July	Fed cuts rates once or twice, but reintroduces a hiking bias

The Fed is about to ease but probably not by as much as the market is expecting

We believe the Fed will move soon to cut interest rates, starting with one 25 basis point (bps) move in July and eventually, by 50bps this year. There is no urgency to ease since the labor market remains strong and, by recent measures, U.S. growth has held up. Nonetheless, the Fed is likely to adjust policy in response to heightened risks to the economic outlook, particularly to global growth and trade, as well as due to the market's declining inflation expectations (**EXHIBIT 4**). Importantly, we do not believe that the Fed is on the precipice of a genuine cutting cycle (that would be our bear case). Rather, we believe they are attempting to fine-tune policy. The rates market currently prices more Fed easing than we anticipate: nearly 100bps of cuts priced over the next 12 months (**EXHIBIT 5**). To the extent that the Fed "underdelivers" on that expectation, we would expect a modest tightening in financial conditions.

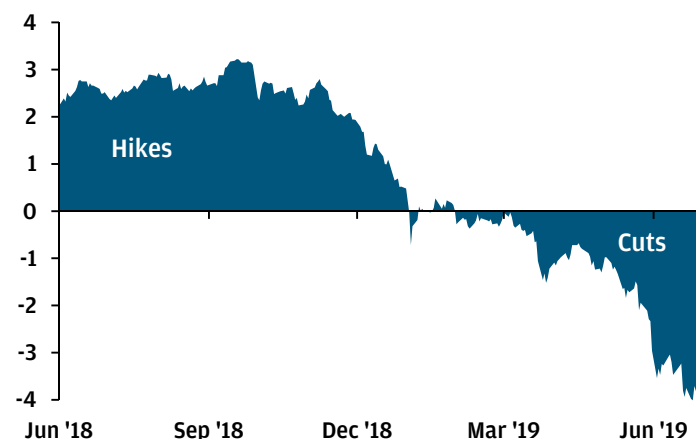
The Fed is concerned about undershooting its inflation mandate

EXHIBIT 4: U.S. MARKET-BASED INFLATION EXPECTATIONS



The market has shifted from hiking mode to cutting mode

EXHIBIT 5: NUMBER OF 25BPS FED MOVES EXPECTED IN THE NEXT 12 MONTHS



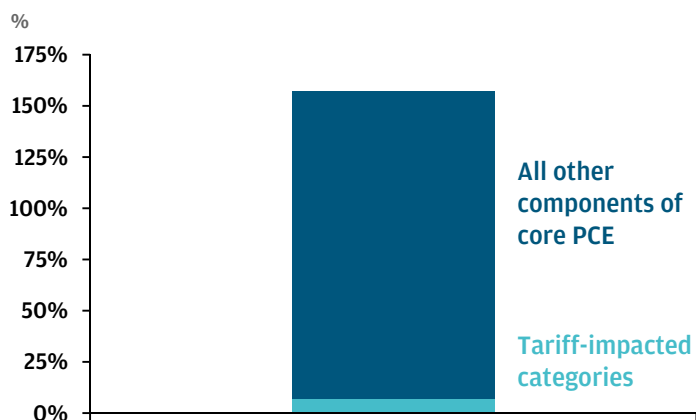
Source: Bloomberg. Data as of June 28, 2019.

The swing factor in our outlook is U.S.-China trade relations

While much has been made of tariffs introduced over the past year, so far their direct impact has been minimal. The effect on U.S. inflation—the main channel through which tariffs hit growth—has essentially been a rounding error (EXHIBIT 6). We suspect that one mitigating factor is country substitution, by which importers are circumventing the higher cost of goods created by tariffs: the U.S. is importing less from China but more from Vietnam, Taiwan and Korea (EXHIBIT 7).

The inflation impact from tariffs has been minimal so far

EXHIBIT 6: CONTRIBUTIONS TO YEAR-OVER-YEAR CORE PCE INFLATION

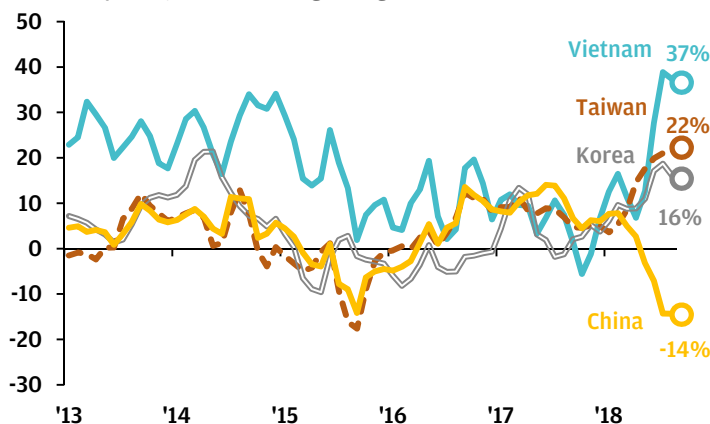


Source: Bureau of Labor Statistics, J.P. Morgan Private Bank Economics. Data as of March 31, 2019. Tariff impacted categories include housekeeping supplies, furniture, floor coverings, major appliances, sewing machines, sports vehicles and auto parts. PCE: Personal Consumption Expenditures.

As U.S. imports from China fall, the rest of Asia is benefiting

EXHIBIT 7: U.S. IMPORTS FROM ASIA

Year-over-year %, 3-month moving average



Source: U.S. Census Bureau, J.P. Morgan Private Bank Economics. Data as of April 30, 2019.

The G20 meeting suggested no imminent escalation in the trade dispute

The U.S.-China presidents' meeting in June yielded little material progress toward a trade deal but talks were to be restarted and additional U.S. tariffs put on hold for the time being. There is popular support in the U.S. for pushing China on its economic policies and trade practices, so we see little urgency for President Trump to accept an agreement. We put a higher probability on some form of agreement as the 2020 U.S. election draws closer. Meanwhile, trade will continue to be a thorn in the side of the global economy. Markets will also be sensitive to whether the dispute escalates beyond tariffs, to include export controls, boycotts or sanctions. The Trump Administration's recent action against the Chinese tech company Huawei was a step in this direction, though some limitations seem likely to be removed following the G20 meeting.

Slowing growth is a global problem and China's stimulus offers little support

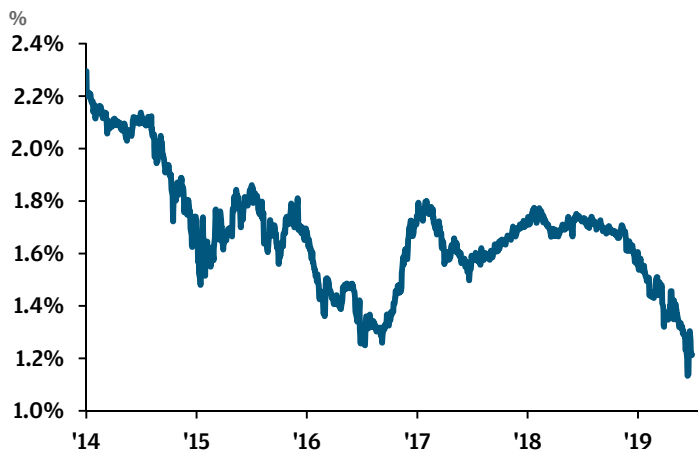
Growth weakness around the world this year has been more a function of sluggish industrial demand than problems with domestically oriented service sectors that have held up better. In the past (in 2010 and 2016), aggressive stimulus from China turned the tide for global manufacturers but this time is different. Yes, China has introduced meaningful stimulus measures over the past year but the government's effort is more consumer-focused and domestically sourced than it was in prior rounds. In other words, its policy measures are helping to stabilize growth within China but are unlikely to turn the tide of the global industrial cycle.

The European Central Bank is back in easing mode

The European Central Bank (ECB) again is concerned about falling market-implied inflation expectations (**EXHIBIT 8**) and acute issues in Europe's weaker economies. For example, Italy's economy is teetering and political uncertainty has weighed on both sentiment and growth. The domestic growth backdrop in the euro area more broadly is less dire (**EXHIBIT 9**) but this does not mean the ECB will remain on hold. ECB President Mario Draghi has made clear that if weakening economic growth and inflation dynamics do not improve, further monetary accommodation will be necessary. The recent nomination of Christine Lagarde as successor to Draghi strengthens our confidence that additional policy accommodation should be forthcoming. The next round of easing is likely to include some combination of rate cuts and more quantitative easing (QE). These steps may help cushion the hit to industrial activity and further support the nonindustrial segments that already look bright.

The ECB is also concerned about undershooting its inflation mandate

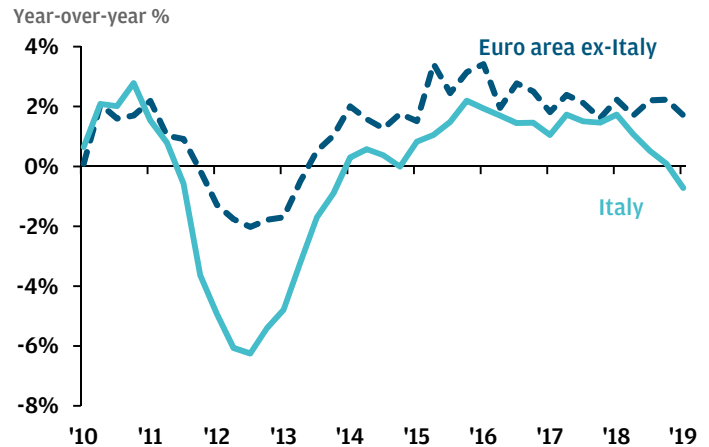
EXHIBIT 8: EURO AREA INFLATION EXPECTATIONS



Source: Bloomberg. Series is the expected inflation (on average) over the five-year period that begins five years from today. Data as of July 1, 2019.

Euro area growth weakness has been concentrated in Italy

EXHIBIT 9: REAL DOMESTIC DEMAND



Source: Statistics Office of the European Communities. Data as of March 31, 2019. Domestic demand is final consumption expenditures plus gross capital formation

EQUITY VIEWS: Some digestion of gains is expected but new highs are still likely

Chris Baggin, Nadia Lovell, Grace Peters and Raymond Cheng

We believe the path forward for global equity markets entails limited upside from current levels, given that multiples are near fair value, negative earnings revisions are on the horizon and ongoing trade uncertainty is likely to weigh on corporate confidence and growth. As our midyear theme states, **Finding growth in a low-growth world** will be key for investors. With limited price upside, dividends become more important to reach total return objectives. Though the most likely path for equities is positive, there are so many investment variables that we also recommend, as our second theme says, continued **Participation with protection**.

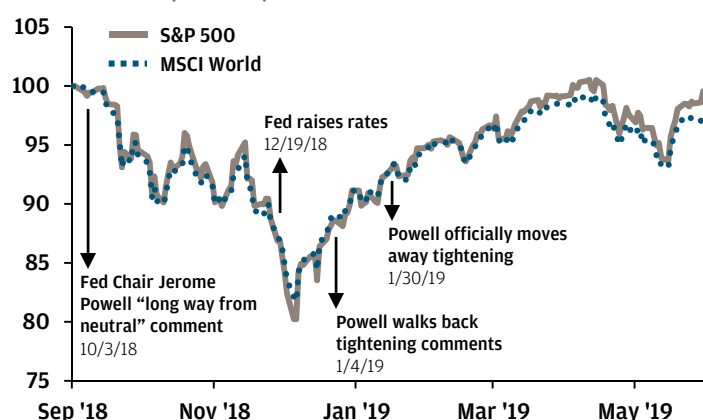
Despite the best first-half returns since 1998, we expect range-bound global markets ahead

After a disappointing end to 2018, global equity markets snapped back from December's multi-year lows (**EXHIBIT 10**). Returns were exceptional in the first half of 2019, with the MSCI World Index up 17%—the best first-half return since 1998. Markets delivered despite global recessionary concerns and ongoing geopolitical tensions—notably the trade skirmish between the U.S. and China—due largely to a coordinated global monetary easing cycle, led by the Fed.

A rapid rally year-to-date leaves markets near fair value

EXHIBIT 10: WORLD EQUITY MARKET RETURNS

Indexed to 100 at peak in September 2018



Source: Bloomberg. Indices used include, S&P 500: SPX Index, MSCI World: MXWO Index. Data as of June 28, 2019.

Our year-end 2019 price targets globally remain largely unchanged from our March Outlook (except for Japan and Asia ex-Japan), and our initial June 2020 targets imply roughly average returns from current levels in developed markets and slightly higher returns in emerging markets (**EXHIBIT 11**). From a risk-reward standpoint, we continue to prefer the U.S. to other developed markets and favor emerging market exposure through Asia ex-Japan. A healthy U.S. consumer and the Fed's likely "insurance" cut should protect the economic expansion cycle and fend off a recession. While we remain neutral on Europe, we like Switzerland as a defensive play. In Asia, trade tensions remain an overhang and tariffs already in place are dragging on growth. China has put a number of measures in place to help offset some of this. With reasonable valuations and light investor positioning, the risk-reward skews positively for China. Within Asia, we prefer India given its pro-growth fiscal policies that are helping to drive double-digit earnings growth.

Expected returns are roughly in line with the long-term average across the developed markets and slightly above average for emerging markets

EXHIBIT 11: GLOBAL EQUITY MARKETS OUTLOOK

Year-end 2019, Midyear 2020

Region	Index	Current Level	December 2019 Equity Outlook						June 2020 Equity Outlook					
			Price level	P/E Forward Multiple	Earnings Growth	Dividend Yield	Price Return ¹	Total Return ¹	Price	P/E Forward Multiple	Earnings Growth	Dividend Yield	Price Return ¹	Total Return ¹
United States	S&P 500	2,942	2,875 - 2,925	16.5x	3 - 4%	2.00%	(2) - (1)%	(1) - 0%	3,050 - 3,150	17.0x	5 - 7%	2.00%	4 - 7%	6 - 9%
Europe	STOXX Europe 600	385	385 - 395	14.0x	3 - 4%	3.70%	0 - 3%	2 - 4%	395 - 405	14.0x	3 - 5%	3.70%	3 - 5%	6 - 9%
Japan	Topix	1,551	1,575 - 1,590	12.5x	6 - 7%	2.40%	2 - 3%	3 - 4%	1,600 - 1,630	12.5x	3 - 4%	2.40%	3 - 5%	5 - 7%
Asia	MSCI Asia ex-Japan	653	670 - 680	12.3x	5 - 6%	2.50%	3 - 4%	6 - 7%	687 - 700	12.3x	5 - 6%	2.50%	5 - 7%	8 - 10%
China	MSCI China	79	83 - 84	10.8x	8 - 9%	2.20%	5 - 6%	7 - 8%	86 - 88	10.8x	9 - 10%	2.20%	9 - 11%	11 - 13%

¹ From June 28, 2019 levels. Represents world headline inflation. FX currency pairs represent price midpoints.

Source: Bloomberg, J.P. Morgan Private Bank. Local currency terms. Data as of June 28, 2019.

U.S.: Digestive period likely in the second half 2019; we see modest upside but new highs by mid-2020

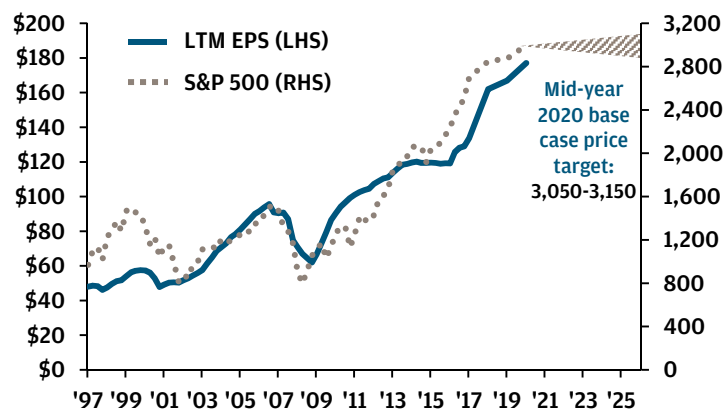
What is now the longest-running bull market expunged December 2018's steep losses and touched new highs, with the S&P 500 gaining 17% in the first half of 2019 (**EXHIBIT 12**). Much of the rally has been sentiment-driven, supported by a more dovish Fed and U.S.-China trade optimism. Valuation multiples have expanded from 13.5x in late December to 16.7x at the end of June. While above the long-term average of roughly 16.5x, we believe the market is within fair value range (16.0x-17.5x), given the low interest rate environment (10-year Treasury yields at roughly 2.0%).

Looking forward, we see little upside over the next six months and our 2019 year-end S&P 500 price target is unchanged at 2,875-2,925. However, we acknowledge that the market could overshoot 3,000 in the near term on optimism about central banks likely easing and potentially improved U.S.-China trade relations. Outside of that, fundamentals are deteriorating as economic growth—the primary driver of S&P 500 sales and earnings growth—is decelerating toward the 1.5%-2.0% range (vs. 3.0% over the last year). This slowdown isn't fully reflected in consensus earnings growth expectations for 2020 which, at around 11%, we view as too high. Current analysts' estimates are calling for roughly 120bps in margin expansion, which we consider unrealistic this late in the business cycle, especially when you combine tariffs' negative impact with a buoyant job market.

Profit margins will likely contract slightly as input costs (i.e. wages, materials, etc.) continue to weigh on profitability. Accordingly, we expect downward revisions to 2020 earnings growth outlook toward our base case of 5%-7%. This earnings downgrade cycle could put pressure on the equity market in coming months and we see a risk of a pullback of about 5%.

Over the long term, S&P 500 performance tracks earnings growth

EXHIBIT 12: S&P 500 INDEX LEVEL & LAST TWELVE MONTHS (LTM) EPS, USD



Source: Bloomberg, Factset, J.P. Morgan Private Bank. Data are as of June 28, 2019. EPS (earnings per share) figures represent JPM PB estimates.

Trade is the wild card with more downside than upside risk

Trade remains a wild card and the risk is asymmetrical—more downside risk from an escalation in tensions than potential upside from a trade deal. **Participation with protection** may be beneficial given the consistently changing trade environment. We estimate tariffs have reduced earnings by about 3 percentage points this year, with the potential for further reduction if tensions escalate. The potential global auto tariffs deadline and U.S.-Mexico-Canada Agreement (USMCA) approval will be closely watched. It remains to be seen if conventional monetary policy actions will be enough to offset the impact of geopolitics.

Investment implications

These overarching uncertainties have caused our 12-month outlook to have fat tails, and therefore, we recommend a barbell approach. Our base case calls for a 60% probability that the S&P 500 reaches our outlook of 3,050-3,150, assuming 5%-7% EPS growth and a 17.0x forward P/E multiple. The likelihood of the tail events is asymmetric. We assign a 30% probability to our downside scenario of 2,500-2,600 and 10% to the upside scenario of 3,250-3,350. The downside scenario is largely predicated on escalating trade tensions and a Fed that is behind the curve, while the upside scenario is dependent on a comprehensive trade deal and the stabilization of international economic growth. In an effort to balance the risks, we want to barbell less-cyclical sectors (health care and staples) with secular growth sectors that have some modest cyclicalities (tech and communication services). From a market cap standpoint, we

continue to prefer large cap over small cap stocks, given their relatively stronger balance sheets and ability to weather an economic slowdown. We also favor quality and dividend growth stocks, which tend to outperform during periods of heightened volatility and lower-than-average expected returns.

Asia: A mixed bag due to trade, though India remains a bright spot

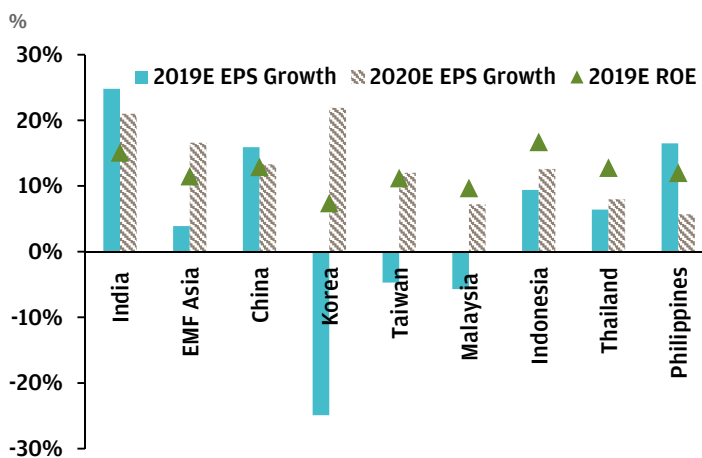
Emerging Asia

We expect Asia's emerging markets to offer the highest rates of return globally over the next 12 months. India should be helped by double-digit earnings growth (EXHIBIT 13), pro-growth fiscal policies (focused on the infrastructure and agricultural sectors) and business and market momentum after the recent re-election of Prime Minister Narendra Modi. The first annual budget of Modi's new term includes plans to increase spending, allow more foreign investment and levy a tax on the wealthy to offset increased deficit spending. While trade tensions remain an overhang, emerging Asia earnings should see support from further policy response, increased domestic orientation and improving shareholder returns.

Reasonable valuations and light investor positioning provide positive risk-reward potential for stocks in China. The U.S.-China trade truce post- the June G20 meeting has provided short-term relief to Asian equities, but China's macro picture continues to weaken, as seen in its disappointing PMI prints. In our view, the uncertainty surrounding trade makes accelerated policy easing critical for business sentiment and earnings to improve.

India's earnings growth is the highest in the region

EXHIBIT 13: ASIAN COUNTRIES' LOCAL CURRENCY EPS GROWTH & ROE

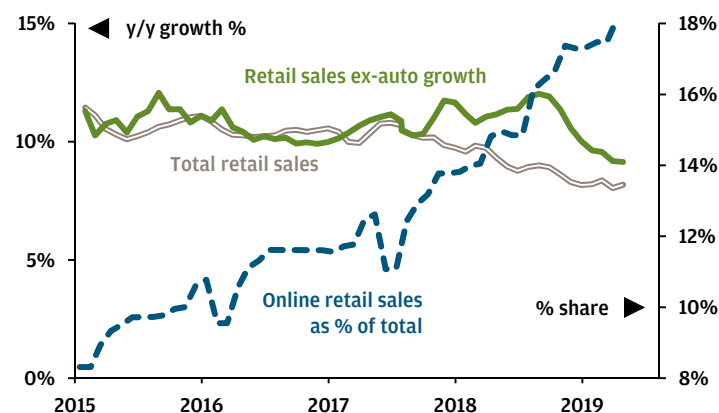


Source: Institutional Brokers' Estimate System, JPMorgan LLC. Data as of June 19, 2019. EPS: earnings per share.

Chinese stimulus is likely to have a more meaningful impact in boosting consumption in the second half of 2019 and into 2020 (**EXHIBIT 14**). Reflecting the uncertain trade outcome, we apply a below-average target forward P/E (price-to-earnings ratio) and establish our 12-month index range for MSCI China at 86-88.

Chinese consumption remains solid while online retail has been resilient

EXHIBIT 14: ONLINE RETAIL SALES GROWTH VS. ONLINE RETAIL SALES AS % OF TOTAL



Source: China National Bureau of Statistics, J.P. Morgan. Data as of June 26, 2019.

Within India, we prefer infrastructure, building materials and rural/agriculture sectors. In China, we prefer exposure through structured investments with downside protection on A shares (the CSI 300 Index). Elsewhere in emerging Asia, we continue to emphasize our preference for consumer-focused companies and we upgrade Industrials, given changing assumptions about the growth of fixed-asset investment. Indonesia is also positioned favorably due to positive fiscal reforms and below-average valuations.

Japan

While we lowered our expectations for equity returns, returns are skewed positively. In our view, the Topix could be poised to rally following the resolution of uncertainty around trade and after the feared consumer tax is imposed in 4Q 2019. Valuations are below average, which is similar to other markets in Asia. There are several strong secular growth stories in the region and Japanese gaming is among our favorite sub-segments, given technological advancements and upgrade cycles from brand leaders.

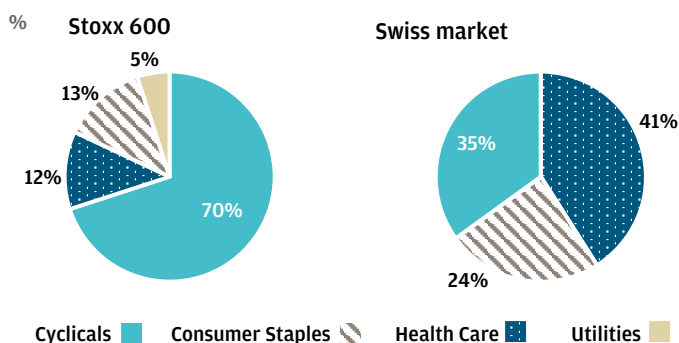
The eurozone macro picture continues to weaken; we recommend positioning defensively in Switzerland

Europe

Weak economic momentum, a value bias and ongoing political risks are headwinds to European earnings growth and risk sentiment. Many multinationals are well positioned for a turn in trade; however, various fiscal and monetary issues in Italy continue to negatively affect the region. Geographically, Switzerland is our preferred defensive market in Europe. (**EXHIBIT 15**). We prefer “self-help” companies, which we define as firms utilizing restructuring to return more cash to shareholders. As an example, we maintain a positive view on the energy sector given capex discipline, structural change and strong yields.

65% of the Swiss market index’s market cap is defensive

EXHIBIT 15: STOXX 600 AND SWISS MARKET INDEX DEFENSIVE VS. CYCLICAL EXPOSURE



Source: Bloomberg, DataStream, J.P. Morgan Private Bank. Data as of June 28, 2019.

FIXED INCOME OUTLOOK: In the face of slowing growth and accommodative central banking, expect low rates

Tom Kennedy & Scott Schnipper

Our fixed income, currencies and commodities outlook informs two of our key mid-year themes: **Harvesting yield** and **Participation with protection**. Here we explain that fixed income outlook: the dangers of reinvestment risk at a time when yields are likely to fall, the implications of central bank easing going global, that protection today comes in many shapes and sizes and our belief that meeting your goals will require investing conservatively but trading opportunistically.

Reinvestment risk is here—staying short may make you feel better but it's not smart investing

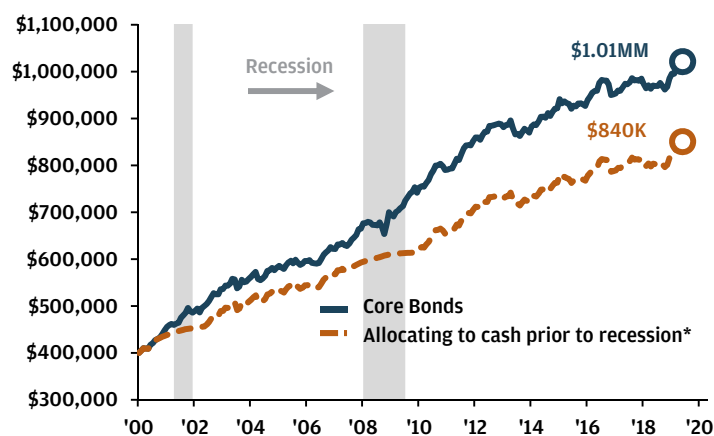
The yield curve has flattened—shorter-term and longer-term bonds currently offer comparable yields. Some people point to this as a reason to embrace cash, cash equivalents and short-duration bonds. We consider this a mistake—and expect the yield curve to steepen. Those embracing cash are putting the focus on current yield instead of where yields will be over their investment horizon. While it's true that short-term fixed income investments have relatively high yields today, we expect the Federal Reserve (Fed) to start cutting policy rates in July. We expect 3-month LIBOR to decline to 2.10% by year-end and the yield curve to steepen.

Staying short may make you feel better, but that's psychology. Financially speaking, cash is unlikely to help you reach your long-term goals. Since the global financial crisis, cash has yielded less than inflation more than 90% of the time. Further, even if you had been able to perfectly predict when recessions would start over the last 20 years and had rebalanced your fixed income portfolio into cash for the entirety of every recession, you would still have underperformed the Bloomberg Barclays US Aggregate Index by about 40% (**EXHIBIT 16**).

Even with perfect hindsight, moving to cash underperformed core bonds

EXHIBIT 16: CONTRIBUTION OF FIXED INCOME PORTION IN 60/40 PORTFOLIO REBALANCED PRIOR TO RECESSIONS

Fixed income portion value, USD



Source: Bloomberg, Haver, J.P. Morgan Private Bank Economics. Data as of April 30, 2019. *Allocating from Core Bonds to cash six months prior to a recession and switching back six months after. Cash is defined as 3m LIBOR. Core Bonds are defined as the Bloomberg Barclays US Aggregate Total Return Index.

Absent a liquidity need, we advocate reducing cash in favor of longer duration

We are making the following recommendations:

- Reduce floating-rate investments, as we expect coupons to decline, in favor of fixed-rate equivalents.
- Preferreds continue to offer compelling risk-adjusted yield; we advocate reducing exposure to short call date preferreds (especially those with low floating-rate resets) in favor of longer-dated call structures or fixed-for-life instruments.
- On the liabilities side, we favor floating rates across the developed world and suggest considering EUR borrowing through floating-rate cross-currency swaps¹.

Protection comes in various shapes and sizes

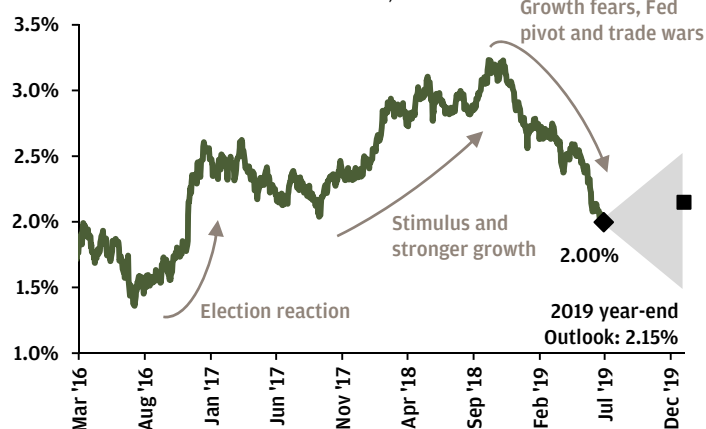
Growth is slowing and the inverted yield curve suggests that we should take steps from a late-cycle stance toward an end-cycle stance. Curve inversion has long been our call and that has occurred. Now the most likely path forward is for the yield curve to steepen. We continue to see forward curve steepeners as a lucrative position to hold as late cycle turns to end cycle. However, year-to-date market moves have changed the economics. Steepeners offer less leverage now than a year ago when we first recommended the position as a portfolio hedge. Consequently, we expect a long gold position to be a more effective portfolio hedge going forward. We see gold trading to USD1,550 per ounce by mid-2020 or higher if a significant growth slowdown looks increasingly likely.

While our macro team is certainly cautious, the bond market is already pricing in a significant growth slowdown as the most likely outcome; we think pricing has gone a bit too far. For those who have de-risked and added duration already, kudos. Unfortunately, most have not, and we advocate doing so regardless of level, in an effort to protect post-crisis gains. We see 10-year Treasury rates at year-end 2019 and mid-year 2020 at 2.15% and 1.75%, respectively; rates are still skewed to the downside.

Right now, we advocate neutral core duration positioning, and if (or when) rates rise a bit toward our fair-value estimates, we will suggest adding to duration. We see value in quality yield: 5-10 year investment grade bonds, longer than 10-year maturity municipal debt and agency mortgages.

U.S. long-term rates have declined further as investors grapple with global growth fears and renewed trade wars

EXHIBIT 17: U.S. 10-YEAR TREASURY YIELD, %



Source: FactSet. Data as of June 30, 2019.

Accommodative central banking has gone global

Central bankers' enemies are slower growth and declining inflation expectations, and the ECB is at the center of this fight. The ECB has reengaged as EUR forward inflation expectations have drawn within a few basis points of historic lows. While some have suggested that the ECB toolbox is limited, the majority of its rules are self-imposed and likely to be adjusted. We expect the ECB to cut the deposit rate another 10bps this year and believe it's likely it will restart QE.

As of June 30, 2019, 25% of the Bloomberg Barclays Global Aggregate Index was trading with a negative yield (**EXHIBIT 18**). The combination of even lower risk-free yields and a restart of QE suggests term and risk premiums will be well supported in Europe. For the euro, the implications are less clear as coordinated central bank actions are likely to result in low volatility in exchange rates. The Fed has more conventional ammunition (rate cuts) to use before considering further asset purchases, and we expect its actions to be the driving force for the U.S. dollar. We see the DXY Dollar Index at 93.5 by mid 2020, which would put EURUSD at 1.15, a slightly stronger euro relative to today.

In search of positive yield in Europe

To find positive yield in the eurozone, one must add interest rate risk and/or credit risk. Waiting for a "better entry point" after rates rise will likely be futile.

The global bond environment is starving for yield

EXHIBIT 18: BARCLAYS GLOBAL AGGREGATE INDEX

	Maturity			
	2yr	5yr	10yr	30yr
Switzerland	Negative yield	Negative yield	Negative yield	Positive yield
Germany	Negative yield	Negative yield	Negative yield	Positive yield
Japan	Negative yield	Negative yield	Negative yield	Positive yield
France	Negative yield	Negative yield	Negative yield	Positive yield
Spain	Negative yield	Negative yield	Positive yield	Positive yield
Italy	Positive yield	Positive yield	Positive yield	Positive yield
UK	Positive yield	Positive yield	Positive yield	Positive yield
U.S.	Positive yield	Positive yield	Positive yield	Positive yield

Sources: Barclays, Bloomberg. Data as of June 30, 2019.

The investment implications of our views include:

- We see value in European bank debt (particularly down in the capital stack) and corporate hybrids.
- Credit-linked notes are an attractive alternative to cash bonds as we can tailor the structure and maturity to clients' specific goals.
- For USD-based investors, European high yield (HY) investments swapped back to USD look attractive; with the swap¹, European HY has a similar yield to U.S. HY but with a higher average credit rating.

An up-in-quality bias is prudent; our mantra is, "Invest conservatively, but trade opportunistically"

The sole purpose of this mantra is to encourage an open mind; volatility breeds overshoots and overshoots introduce opportunities. Credit globally had a great start to 2019. That leads us to recommend adding hedges to lock in gains and/or take profits in riskier credits. Just about every one of our fundamental screens and valuation lenses suggest an up-in-quality bias is prudent. Over the next 12 months, we expect carry-like total returns in U.S. investment grade and less than carry in U.S. high yield and emerging market debt.

That said, not all high yield and emerging market debt is created equal and unconstrained fixed income strategies are a compelling way to add yield enhancement while remaining nimble. In Asia, we favor Chinese issuers with strong government sponsorship, Indian corporates tied to macro reform and quasi-sovereign Indonesian credits that offer yield enhancement over sovereigns.

¹ This is a structured product which involves derivatives. Investors should not invest in it unless they fully understand and are willing to assume the risks associated with it. If investors are in any doubt about the risks involved in investing in a structured product, they may clarify with their usual J.P. Morgan representative or seek independent professional advice. No person should make an investment decision on the basis of this document. Such decision should be made solely on the basis of the information contained in the relevant offering documentation for a particular trade. Investing in fixed income products is subject to certain risks, including interest rate, credit, inflation, call, prepayment, and reinvestment risk.

INDEX DEFINITIONS:

- 3-month LIBOR: London Interbank Offered Rate of LIBOR with respect to a three-month period for deposits of United States Dollars as reported by Bloomberg Financial Markets.
- Bloomberg Barclays Global Aggregate Index: This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers
- Bloomberg Barclays US Aggregate Index: market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type.
- CSI 300 Index: capitalization-weighted stock market index designed to replicate the performance of top 300 stocks traded in the Shanghai and Shenzhen stock exchanges.
- DXY Dollar Index: value of the United States dollar relative to a basket of foreign currencies, often referred to as a basket of U.S. trade partners' currencies.
- MSCI Asia ex-Japan: captures large and mid cap representation across 2 of 3 Developed Markets countries (excluding Japan) and 9 Emerging Markets countries in Asia.
- MSCI China: captures large and mid-cap representation across China.
- MSCI World Index (MXWO): includes collection of stocks of all the developed markets in the world, as defined by MSCI
- S&P 500 Index: market-capitalization-weighted index of the 500 largest U.S. publicly traded companies
- STOXX 600: stock index of European stocks
- Swiss market index: 20 of the largest and most liquid Swiss Performance Index (SPI) large- and mid-cap stocks.
- Topix: free-float adjusted market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the TSE First Section

This material is for informational purposes only, and may inform you of certain products and services offered by J.P. Morgan's wealth management businesses, part of JPMorgan Chase & Co. ("JPM"). **Please read all Important Information.**

GENERAL RISKS & CONSIDERATIONS

Any views, strategies or products discussed in this material may not be appropriate for all individuals and are subject to risks. **Investors may get back less than they invested, and past performance is not a reliable indicator of future results.** Asset allocation does not guarantee a profit or protect against loss. Nothing in this material should be relied upon in isolation for the purpose of making an investment decision. You are urged to consider carefully whether the services, products, asset classes (e.g., equities, fixed income, alternative investments, commodities, etc.) or strategies discussed are suitable to your needs. You must also consider the objectives, risks, charges and expenses associated with an investment service, product or strategy prior to making an investment decision. For this and more complete information, including discussion of your goals/situation, contact your J.P. Morgan representative.

The price of equity securities may rise or fall due to the changes in the broad market or changes in a company's financial condition, sometimes rapidly or unpredictably. Equity securities are subject to "stock market risk," meaning that stock prices in general may decline over short or extended periods of time.

In general, the bond market is volatile, bond prices rise when interest rates fall and vice versa. Longer term securities are more prone to price fluctuation than shorter term securities. Any fixed income security sold or redeemed prior to maturity may be subject to substantial gain or loss. Dependable income is subject to the credit risk of the issuer of the bond. If an issuer defaults no future income payments will be made.

NON-RELIANCE

Certain information contained in this material is believed to be reliable; however, JPM does not represent or warrant its accuracy, reliability or completeness, or accept any liability for any loss or damage (whether direct or indirect) arising out of the use of all or any part of this material. No representation or warranty should be made with regard to any computations, graphs, tables, diagrams or commentary in this material, which are provided for illustration/reference purposes only. The views, opinions, estimates and strategies expressed in this material constitute our judgment based on current market conditions and are subject to change without notice. JPM assumes no duty to update any information in this material in the event that such information changes. Views, opinions, estimates and strategies expressed herein may differ from those expressed by other areas of JPM, views expressed for other purposes or in other contexts, and **this material should not be regarded as a research report.** Any projected results and risks are based solely on hypothetical examples cited, and actual results and risks will vary depending on specific circumstances. Forward-looking statements should not be considered as guarantees or predictions of future events.

Nothing in this document shall be construed as giving rise to any duty of care owed to, or advisory relationship with, you or any third party. Nothing in this document shall be regarded as an offer, solicitation, recommendation or advice (whether financial, accounting, legal, tax or other) given by J.P. Morgan and/or its officers or employees, irrespective of whether or not such communication was given at your request. J.P. Morgan and its affiliates and employees do not provide tax, legal or accounting advice. You should consult your own tax, legal and accounting advisors before engaging in any financial transactions.

**IMPORTANT INFORMATION ABOUT YOUR INVESTMENTS AND POTENTIAL CONFLICTS OF INTEREST**

Conflicts of interest will arise whenever JPMorgan Chase Bank, N.A. or any of its affiliates (together, “J.P. Morgan”) have an actual or perceived economic or other incentive in its management of our clients’ portfolios to act in a way that benefits J.P. Morgan. Conflicts will result, for example (to the extent the following activities are permitted in your account): (1) when J.P. Morgan invests in an investment product, such as a mutual fund, structured product, separately managed account or hedge fund issued or managed by JPMorgan Chase Bank, N.A. or an affiliate, such as J.P. Morgan Investment Management Inc.; (2) when a J.P. Morgan entity obtains services, including trade execution and trade clearing, from an affiliate; (3) when J.P. Morgan receives payment as a result of purchasing an investment product for a client’s account; or (4) when J.P. Morgan receives payment for providing services (including shareholder servicing, recordkeeping or custody) with respect to investment products purchased for a client’s portfolio. Other conflicts will result because of relationships that J.P. Morgan has with other clients or when J.P. Morgan acts for its own account.

Investment strategies are selected from both J.P. Morgan and third-party asset managers and are subject to a review process by our manager research teams. From this pool of strategies, our portfolio construction teams select those strategies we believe fit our asset allocation goals and forward-looking views in order to meet the portfolio’s investment objective.

As a general matter, we prefer J.P. Morgan managed strategies. We expect the proportion of J.P. Morgan managed strategies will be high (in fact, up to 100%) in strategies such as, for example, cash and high-quality fixed income, subject to applicable law and any account-specific considerations.

While our internally managed strategies generally align well with our forward-looking views, and we are familiar with the investment processes as well as the risk and compliance philosophy of the firm, it is important to note that J.P. Morgan receives more overall fees when internally managed strategies are included. We offer the option of choosing to exclude J.P. Morgan managed strategies (other than cash and liquidity products) in certain portfolios.

The Six Circles Funds are U.S.-registered mutual funds managed by J.P. Morgan and sub-advised by third parties. Although considered internally managed strategies, JPMC does not retain a fee for fund management or other fund services.

LEGAL ENTITY, BRAND & REGULATORY INFORMATION

In the **United States**, bank deposit accounts and related services, such as checking, savings and bank lending, are offered by **JPMorgan Chase Bank, N.A.** Member FDIC.

JPMorgan Chase Bank, N.A. and its affiliates (collectively “**JPMCB**”) offer investment products, which may include bank-managed investment accounts and custody, as part of its trust and fiduciary services. Other investment products and services, such as brokerage and advisory accounts, are offered through **J.P. Morgan Securities LLC (“JPMS”)**, a member of FINRA and SIPC. Annuities are made available through Chase Insurance Agency, Inc. (CIA), a licensed insurance agency, doing business as Chase Insurance Agency Services, Inc. in Florida. JPMCB, JPMS and CIA are affiliated companies under the common control of JPMorgan Chase & Co. Products not available in all states.

In **Luxembourg**, this material is issued by J.P. Morgan Bank Luxembourg S.A (JPMBL), with registered office at European Bank and Business Centre, 6 route de Treves, L-2633, Senningerberg, Luxembourg. R.C.S Luxembourg B10.958. Authorized and regulated by Commission de Surveillance du Secteur Financier (CSSF) and jointly supervised by the European Central Bank (ECB) and the CSSF. J.P. Morgan Bank Luxembourg S.A. is authorized as a credit institution in accordance with the Law of 5th April 1993. In the **United Kingdom**, this material is issued by J.P. Morgan Bank Luxembourg S.A., London Branch. Prior to Brexit (Brexit meaning that the United Kingdom leaves the European Union under Article 50 of the Treaty on European Union, or, if later, loses its ability to passport financial services between the United Kingdom and the remainder of the EEA), J.P. Morgan Bank Luxembourg S.A., London Branch is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority. Details about the extent of our regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from us on request. In the event of Brexit, in the United Kingdom, J.P. Morgan Bank Luxembourg S.A., London Branch is authorized by the Prudential Regulation Authority, subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. In **Spain**, this material is distributed by J.P. Morgan Bank Luxembourg S.A., Sucursal en España, with registered office at Paseo de la Castellana, 31, 28046 Madrid, Spain. J.P. Morgan Bank Luxembourg S.A., Sucursal en España is registered under number 1516 within the administrative registry of the Bank of Spain and supervised by the Spanish Securities Market Commission (CNMV). In **Germany**, this material is distributed by J.P. Morgan Bank Luxembourg S.A., Frankfurt Branch, registered office at Taunustor 1 (TaunusTurm), 60310 Frankfurt, Germany, jointly supervised by the Commission de Surveillance du Secteur Financier (CSSF) and the European Central Bank (ECB), and in certain areas also supervised by the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin). In **Italy**, this material is distributed by J.P. Morgan Bank Luxembourg S.A., Milan Branch, registered office at Via Cantena Adalberto 4, Milan 20121, Italy and regulated by Bank of Italy and the Commissione Nazionale per le Società e la Borsa (CONSOB). In addition, this material may be distributed by **JPMorgan Chase Bank, N.A. (“JPMCB”), Paris branch**, which is regulated by the French banking authorities Autorité de Contrôle Prudentiel et de Résolution and Autorité des Marchés Financiers or by **J.P. Morgan (Suisse) SA**, which is regulated in Switzerland by the Swiss Financial Market Supervisory Authority (FINMA).



In **Hong Kong**, this material is distributed by **JPMCB, Hong Kong branch**. JPMCB, Hong Kong branch is regulated by the Hong Kong Monetary Authority and the Securities and Futures Commission of Hong Kong. In Hong Kong, we will cease to use your personal data for our marketing purposes without charge if you so request. In **Singapore**, this material is distributed by JPMCB, Singapore branch. **JPMCB, Singapore branch** is regulated by the Monetary Authority of Singapore. Dealing and advisory services and discretionary investment management services are provided to you by JPMCB, Hong Kong/Singapore branch (as notified to you). Banking and custody services are provided to you by JPMCB Singapore Branch. The contents of this document have not been reviewed by any regulatory authority in Hong Kong, Singapore or any other jurisdictions. You are advised to exercise caution in relation to this document. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice. For materials which constitute product advertisement under the Securities and Futures Act and the Financial Advisers Act, this advertisement has not been reviewed by the Monetary Authority of Singapore.

J.P. Morgan Chase Bank, N.A. (JPMCBNA) (ABN 43 074 112 011/AFS Licence No: 238367) is regulated by the Australian Securities and Investment Commission and the Australian Prudential Regulation Authority. Material provided by JPMCBNA in Australia is to “wholesale clients” only. For the purposes of this paragraph the term “wholesale client” has the meaning given in section 761G of the Corporations Act 2001 (Cth). Please inform us if you are not a Wholesale Client now or if you cease to be a Wholesale Client at any time in the future. JPMS is a registered foreign company (overseas) (ARBN 109293610) incorporated in Delaware, U.S.A. Under Australian financial services licensing requirements, carrying on a financial services business in Australia requires a financial service provider, such as J.P. Morgan Securities LLC (JPMS), to hold an Australian Financial Services Licence (AFSL), unless an exemption applies. JPMS is exempt from the requirement to hold an AFSL under the Corporations Act 2001 (Cth) (Act) in respect of financial services it provides to you, and is regulated by the SEC, FINRA and CFTC under U.S. laws, which differ from Australian laws. Material provided by JPMS in Australia is to “wholesale clients” only. The information provided in this material is not intended to be, and must not be, distributed or passed on, directly or indirectly, to any other class of persons in Australia. For the purposes of this paragraph the term “wholesale client” has the meaning given in section 761G of the Act. Please inform us immediately if you are not a Wholesale Client now or if you cease to be a Wholesale Client at any time in the future.

This material has not been prepared specifically for Australian investors. It:

- may contain references to dollar amounts which are not Australian dollars;
- may contain financial information which is not prepared in accordance with Australian law or practices;
- may not address risks associated with investment in foreign currency denominated investments; and
- does not address Australian tax issues.

With respect to countries in **Latin America**, the distribution of this material may be restricted in certain jurisdictions. We may offer and/or sell to you securities or other financial instruments which may not be registered under, and are not the subject of a public offering under, the securities or other financial regulatory laws of your home country. Such securities or instruments are offered and/or sold to you on a private basis only. Any communication by us to you regarding such securities or instruments, including without limitation the delivery of a prospectus, term sheet or other offering document, is not intended by us as an offer to sell or a solicitation of an offer to buy any securities or instruments in any jurisdiction in which such an offer or a solicitation is unlawful. Furthermore, such securities or instruments may be subject to certain regulatory and/or contractual restrictions on subsequent transfer by you, and you are solely responsible for ascertaining and complying with such restrictions. To the extent this content makes reference to a fund, the Fund may not be publicly offered in any Latin American country, without previous registration of such fund’s securities in compliance with the laws of the corresponding jurisdiction. Public offering of any security, including the shares of the Fund, without previous registration at Brazilian Securities and Exchange Commission-CVM is completely prohibited. Some products or services contained in the materials might not be currently provided by the Brazilian and Mexican platforms.

References to “J.P. Morgan” are to JPM, its subsidiaries and affiliates worldwide. “J.P. Morgan Private Bank” is the brand name for the private banking business conducted by JPM.

This material is intended for your personal use and should not be circulated to or used by any other person, or duplicated for non-personal use, without our permission. If you have any questions or no longer wish to receive these communications, please contact your J.P. Morgan representative.

JPMPB-II-MidyearOutlook_July2019