Forecast
Market Outlooks

Q4 2021

Forecasts Quarter 4, 2021

Global Economic Outlook

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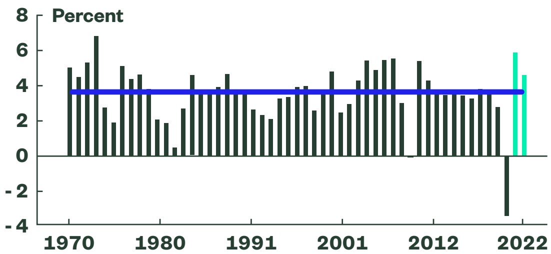
Figure 1
Global Recovery on Track

World, GDP Growth
World, GDP Growth Forcast
Long Term Average Growth (3.65%)



Source: State Street Global Advisors Economics, Macrobond, International Monetary Fund. The above forecast is an estimate based on certain assumptions and analysis made by the State Street Global Advisors Economics Team. There is no guarantee that the estimates will be achieved.

- The global economy continued to recover through the latest quarter, although the recovery remains uneven across countries and sectors amid ongoing COVID-19 difficulties and congestion in supply chains.
- We raised our inflation forecasts for 2021 and 2022. Although the cyclical peak may be passing, inflationary pressures seem poised to linger into next year, focusing the spotlight on central banks' response to the changing landscape.

Emerging Markets Outlook

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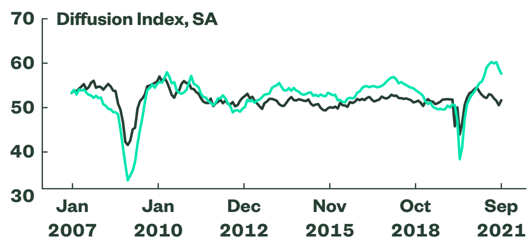
Figure 2
EM Lags DM In COVID Recovery

EM Manufacturing PMI
DM Manufacturing PMI



Source: State Street Global Advisors Economics, Macrobond, IHS Markit.

- Emerging markets have remained in the eye of the COVID-19 storm as the spread of virus variants has contributed to an uneven recovery, notwithstanding a significant improvement in vaccination rates.
- We have trimmed our EM GDP expansion forecast for 2022, driven by the likely impact of Evergrande's difficulties on Chinese growth in 2022.

Global Capital Markets

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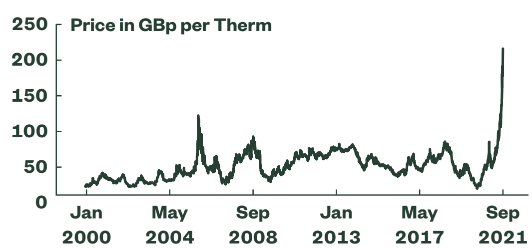
Figure 3
UK Natural Gas Prices Spike Higher



Source: State Street Global Advisors, Bloomberg Finance L.P., as of September 30, 2021. Past performance is not a reliable indicator of future performance.

- Equity markets continue to look attractive despite recent weakness, but with moderating risk regimes, cyclical influences and earnings indicators, a more cautious stance is warranted.
- Commodities continue to look attractive, although the recent price frenzies seen in certain markets are unlikely to be sustained.

Global Economic Outlook

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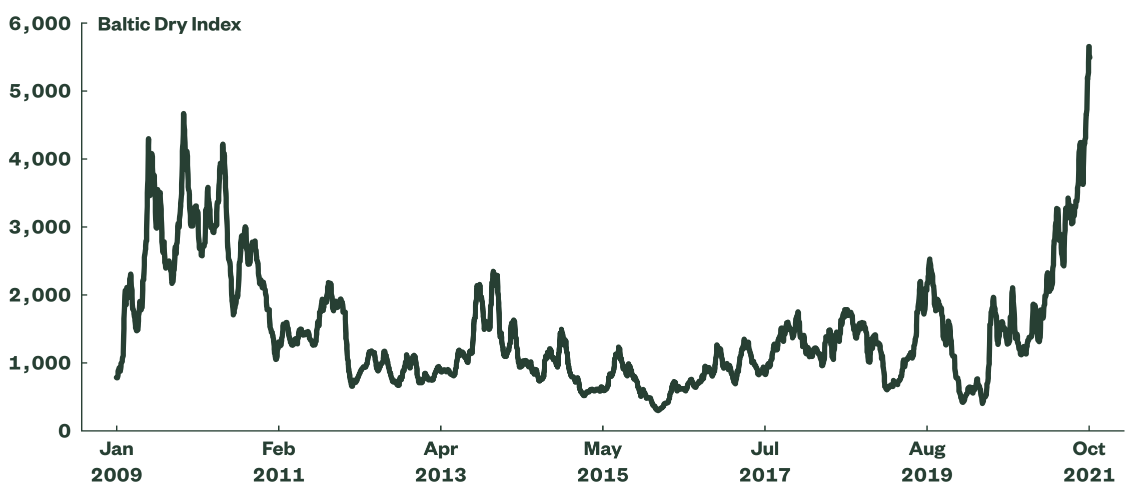
The global economic recovery remains in place, notwithstanding the ongoing impact of supply chain delays, stubbornly higher inflation and still-high levels of COVID-19 infections in many countries. Robust overall demand continues to underpin our global growth forecasts, which remain largely unchanged for 2021 and 2022.

Life After Peak Growth, Peak Inflation, and Peak Policy Accommodation

Given all that has transpired in the global economy over the last six months, it is perhaps surprising that our global growth forecasts have changed very little since March. In June, we raised our 2021 global growth forecast by just two tenths to 5.9% and the September update left that number unchanged. In other words, incoming data has confirmed expectations for a robust recovery that nonetheless remains constrained by COVID-19 and supply chain limitations. The recovery also remains highly uneven across countries and sectors, and — particularly with regard to the labor market — remains incomplete. A noticeable, but not dramatic, downgrade to China's 2022 growth prospects (now at 5.0%) drove a slight reduction in the 2022 global GDP growth forecast despite modest upgrades in several advanced economies. Even so, the big picture remains one of rapid, well-above potential global growth for a second consecutive year.

Figure 4
Elevated Shipping Costs Exacerbate Supply Chain Problems, Inflation

World Baltic Exchange Shipping Dry Index (USD)



Source: State Street Global Advisors, Baltic Exchange as of September 2021.

Inflation forecasts for 2021 have been raised again across most advanced economies, and in some cases, so too have the 2022 projections. Even if the cyclical peak in inflation might well be close at hand (if not already behind us), inflationary pressures seem poised to linger well into next year. We suspect that the intense debate around the transient (or otherwise) nature of the current inflation episode will still be raging a year from now, and not just in the United States. We are especially watching inflation expectations and wages for signals about a potentially more inflationary regime going forward.

Against a backdrop of strong growth and perky inflation, developed market central banks likely take steps to wind down asset purchases. We expect some of them — particularly the Bank of England, the Bank of Canada, and the Fed — to also deliver at least one rate hike before the end of 2022. Emerging market central banks have been further ahead on the policy normalization path, with broad and substantive rate hikes that sought to keep pace with rising inflation.

The big macro story is that the global economy is moving past peak growth, peak inflation, and peak policy accommodation. Even so, this expansion likely has a lot further to go and 2022 is shaping up to be another year of far above potential growth. The pattern of growth will gradually shift, and we expect the US growth advantage to narrow sharply. As growth rotates, will investment flows follow?

United States: Peaking, But Still Robust

The data flow of the last few months has validated our top line assessment of the US economy. Since June, the Bloomberg consensus for 2021 US growth has retreated from 6.6% to 5.9%. We stood at 5.9% in June and have now trimmed that forecast to 5.8% — essentially a rounding difference. But we always emphasized that our below-consensus forecast was a reflection of supply constraints rather than demand problems. Indeed, we wrote three months ago that the consumer spending surge that followed the December and March fiscal stimulus rounds was "exacerbating supply chain constraints as well as inflationary pressures, and may lead to some postponement of consumption from here on, either by choice or by necessity."

This is exactly what has since transpired. It is also why we had maintained our upside to consensus views on 2022 US growth for many months and why we actually raised that forecast again in September (to 4.4%). Admittedly, next year's growth may look better on paper than it will feel in real life as the headline GDP print will be flattered by substantial inventory accumulation. Consumer spending growth is actually poised to halve, although given its extraordinarily high level, a further 4.0% gain still represents an incredible outcome. The consumer spending story over the next year will also increasingly be one of rotation away from goods and into services.

Housing sector activity has moderated lately, with residential investment actually contracting for the first time in a year during the second quarter. High prices and supply constraints are to blame and while lumber prices have fully normalized following their earlier parabolic rise, labor, land, and other supplies remain tight and builders appear to be intentionally managing down housing starts. Nevertheless, housing demand conditions remain healthy and we anticipate positive contributions from residential investment in coming quarters. Structures investment is starting to recover, although with ongoing challenges in oil exploration (rig counts are still down by 35% compared with the start of 2020) and parts of commercial real estate, it may not be until 2022 that the sectors experience meaningful growth. Business equipment and IP investments should continue to do well. Inventory accumulation is sorely needed but has been constrained so far by the sheer strength of demand; it should, however, begin in earnest in the coming months.

Inflation Spike: How Transitory?

The inflation spike has proven even more intense and persistent than we had previously anticipated. Although leading inflation indicators are broadly peaking now, and the US inflation peak itself may be behind us, the downslope will likely be quite mild and elongated. We are looking for “inflation rotation” as we move into 2022. As inflationary pressures moderate in “re-opening” categories such as hotels or “supply-chain bottlenecks” categories like automobiles, we look to rent inflation and broader housing costs to keep inflation elevated next year. Even so, it is possible (and even likely) that headline inflation dips below 2.0% year-on-year (y/y) at some point in mid-2022 due to base effects. We would caution against concluding that such a dip would permanently settle the inflation debate in favor of the “transient” view. To us, the question of whether we are moving toward a more inflationary regime hinges on the behavior of inflation expectations and the behavior of wages. We’ll continue to watch these two indicators very closely.

Fed Tapering Nears

The Fed has provided ample policy accommodation throughout the COVID crisis but, acknowledging progress toward the employment and inflation goals, has all but signaled that it would start to taper asset purchases by the end of this year. This, too, was in line with our expectations. Although Chair Jerome Powell has gone to great lengths to caution against assuming a “direct link” between the timing for taper and the timing for rate lift-off, we still consider the two as sequential stops along the same route toward policy normalization. With asset purchases winding down by mid-2022, we are penciling in one rate hike in 2022 and acknowledge the possibility of another.

Eurozone: Mixed Developments

The eurozone has been an interesting case study this year. On the one hand, this was perhaps where our views had been most divergent relative to consensus back in March. We had embraced a positive view of regional growth on the assumption — long since validated — that vaccine deployment would be scaled up quickly once supplies became available. Moreover, we expected that this would drive a marked acceleration in growth from Q2 onward as consumers started to unleash excess savings. That general narrative held true as both first and second quarter GDP surprised positively, but the country-by-country outcomes were a bit more nuanced.

Germany Surprises

On the whole, our top-line 2021 forecast hasn’t changed much over the last six months: we started at 5.5% in March, went to 5.4% in June, and settled at 5.2% in September. Consensus moved in the opposite direction, as did the ECB staff forecasts that stood at 4.0% in March but reached 5.0% by September. What forced our modest downgrade was the weak flow of German data so far — if we’ve been surprised by anything, it has been this. We had expected more vibrancy in consumer spending, but whether due to domestic political changes, or innate cautiousness, or mobility constraints, German consumer spending has undershot our expectations. Supply chain challenges in auto manufacturing also appear to have lent a heavier blow to German economic activity than had been the case elsewhere. Suffice to say, we’ve lowered Germany’s 2021 growth forecast quite sharply, from 4.4% to 3.6% this round. The hit is largely offset by a sizable upward revision to 2022. The hit to regional growth was mitigated by slight upgrades to France and Italy, among others.

Inflation Tame Enough for ECB

The eurozone's inflation deficit has been a perennial problem in the context of low growth and weak demand. Meeting the inflation target sustainably will remain very difficult, but cyclical and technical factors will likely lift headline inflation to 2.3% this year (from 0.3% in 2020). We have raised our 2022 inflation forecast as well, up to 1.8% compared with 1.6% in June. However, Europe's inflation episode is likely to be both less intense and less durable than in the United States, allowing the ECB to retain a dovish stance for longer and to lag the Fed's rate normalization.

United Kingdom: Breaking Free

We've maintained an upside-to-consensus view of UK growth since early this year, but with consensus having moved up sharply since spring, that gap has now largely been closed. Our own forecasts are little changed since June (our 2021 growth estimate went up a tenth to 7.0% and 2022 went up two tenths to 5.6%) as we continue to anticipate a gradual release of pent-up consumer demand as mobility restrictions ease. Unfortunately, COVID-19 remains a risk and, despite the UK's leading vaccination status, we remain concerned about the possibility of intermittent restrictions through year-end. This is why our expectations for consumer spending during the second half of the year remain quite tame.

Fixed investment in the UK has been weak since the Brexit referendum. It contracted 8.8% last year and in level terms it is now roughly where it was in 2015. Investment incentives included in the new budget, combined with the broader recovery in demand and reduction in uncertainty now that Brexit is complete, should theoretically help revive investment spending going forward — but the going has been slow thus far. Importantly, there remains considerable uncertainty about the new underlying path of investment in the post-Brexit world. What is urgently required is some inventory rebuilding. The inventory drawdown during COVID-19 has been ferocious almost everywhere, but the drawdowns seen in the UK had long preceded COVID-19 and the resulting drag on GDP growth has been extremely large. This represents an upside risk to 2022 growth forecasts, assuming global supply chains normalize.

Back in March, our forecast for 1.9% inflation in 2021 was so far above incoming data that we felt no need to change it in June. However, we upped that projection by three tenths to 2.2% in September on account of the stronger-than-expected August inflation print and the intense surge in global gas prices that could keep domestic energy costs elevated for a while. It is partly due to this factor that we've also raised the 2022 inflation forecast quite sharply to 2.8%. Other factors reflect higher-than-expected wage inflation and the increased likelihood that firms would seek to pass on some of the costs onto customers.

Bank of England Poised to Tighten

With risks to the outlook moderating alongside vaccinations, the need for extraordinary monetary policy accommodation has diminished. Early in the crisis, the Bank of England (BoE) cut the Bank Rate by 65 basis points to 0.1% and increased the quantitative easing (QE) program from £435 billion to £745 billion (and later to £875 billion). It also engaged in various liquidity operations and extended real-economy lending incentives. The BoE has also added negative interest rates to its toolkit, having instructed the Prudential Regulatory Agency (PRA) in February to "engage with PRA-regulated firms to ensure they commence preparations in order to be ready to implement a negative Bank Rate at any point after six months." However, this is a tool for the next business cycle, not this one.

In fact, improving economic conditions have already led the Bank's Monetary Policy Committee (MPC) to conclude that the pace of purchases could be "slowed somewhat". At its September meeting, the MPC maintained all policy parameters unchanged but we were reminded that "the MPC's remit is clear that the inflation target applies at all times, reflecting the primacy of price stability in the UK monetary policy framework." The MPC also believes that, despite ongoing uncertainties, that the case for some "modest tightening of monetary policy over the forecast horizon" appears to have strengthened. We concur. We had already expected the BoE to start raising rates in 2022, but instead of one hike we now expect two, to bring the Bank rate to 0.5% by the end of next year.

Japan: Abe/Suga Policy Line To Persist

A year after the unexpected resignation of Prime Minister Shinzo Abe, Japan is once again in the midst of a political transition. The first priority of the incoming Kishida administration will be enhance the COVID-19 response to facilitate the eventual reopening of the economy. After a slow start, Japan's vaccination rate has skyrocketed over the last two months, with the country now a world leader in terms of vaccination rates.

However, given the hit to third-quarter growth, we have downgraded the 2021 growth projection by 0.4 percentage points to 2.6%. The outlook for 2022 remains positive, as consumption starts to normalize, supply bottlenecks fade and additional fiscal stimulus kicks in. We believe that real GDP should grow by 3.0% next year.

Unlike almost everywhere else, there is little in the way of inflationary pressures in Japan. In fact, base year changes and overall softer demand caused us to slightly downgrade the 2021 projection to -0.1% y/y. In 2022, the impact of these idiosyncratic factors should dissipate to some extent. But underlying inflation is unlikely to consistently top 1% over the next several years. The output gap should narrow, but it is more likely to remain negative throughout 2021–22. A weak labor market and sluggish wage growth will also keep a lid on inflationary pressures in the longer term. We expect inflation to edge up to 0.5% y/y by the end of 2022, leaving it still some distance from what the Bank of Japan would want to see.

BoJ Policy Likely To Hold

We expect the status quo to be maintained on the monetary policy front, with Bank of Japan Governor Haruhiko Kuroda serving until the end of his term in April 2023. In the latest monetary policy meeting, the BoJ kept all policy parameters unchanged, including yield curve control, asset purchase programs, and forward guidance. The BoJ also laid out details of the Green Financing Program, of which the initial outline was announced at the previous meeting. Financial institutions who disclose information on the four thematic areas — governance, strategy, risk management, and metrics and targets — will be eligible for loans at a 0% rate of interest for one year. The investments and loans eligible for financing include green loans and bonds (including sustainability bonds) and transition finance. The operation will commence in late December, and will be offered twice a year until March 31, 2031, as long as it does not interfere with the smooth conduct of market operations.

Emerging Markets Outlook

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COVID-19 case numbers persisted at higher levels for longer in many emerging markets, but vaccination rates have improved significantly. This will likely translate into further steps towards normalization of economic activity, although we have trimmed our growth forecast for 2022.

Emerging Markets: When China Sneezes

The incoming macro data out of emerging markets (EM) remains mixed, mirroring COVID-19 developments. The “rotating hot spot” pattern we identified months ago remains an apt description of the present virus reality, despite much improved vaccination rates. Concerns around vaccine efficacy against new variants will likely persist for some time and could reduce the signal value from vaccination rates in coming months. Nonetheless, despite these challenges, there is undeniable progress against the disease, progress that will translate into further steps towards normalization of economic activity. In other words, the COVID battle has not been won yet, but it is being won, one day and one week at a time.

By and large, our forecasts for the emerging markets group as a whole have held up well in the face of incoming data. Perhaps most importantly, we made no changes to our below-consensus 2021 growth forecast of 7.9% for China, but neither do we believe there is much downside to this projection despite the Evergrande debacle. Nevertheless, even though we anticipate an effective ringfencing of the Evergrande debt problems, it seems inevitable that there will be some negative spillover effect on 2022 GDP growth, which we have lowered to 5.0% from 5.6% three months ago. This, in turn, drives a 0.3 percentage point downgrade to our 2022 EM growth forecast.

Unlike their developed market counterparts, emerging market central banks are considerably further ahead on the monetary policy normalization path. First and foremost, this has been driven by concerns around inflation, particularly in the context of non-reserve currencies and high debt burdens. The upside here relative to past cycles may be that by the time DM central banks finally start raising rates in 2022, the impact on EM currencies may be relatively contained.

Global Capital Markets Outlook

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Investment Solutions Group

The outlook for many growth-oriented asset classes continues to appear positive, albeit less so than in the recent past. Broad measures of sentiment and risk indicators still look reasonable, and while there has been some deceleration in business cycle indicators we continue see a favorable environment for stocks and commodities.

A (Less) Bullish Outlook

The relatively uninterrupted progress that equity markets had managed to achieve since the depths of the COVID-induced market panic have started to encounter some more serious, though not debilitating, disturbances. The MSCI All Country World Index, for instance, registered its first quarterly loss since the beginning of 2020 — even if the total return concession was just barely in the red. A confluence of slower — and at times disappointing — economic data, aggressive macroprudential and regulatory interventions in China, and collective investor anxiety surrounding monetary policy withdrawal all served to reinforce a more tentative tone to trading as the third quarter came to a close.

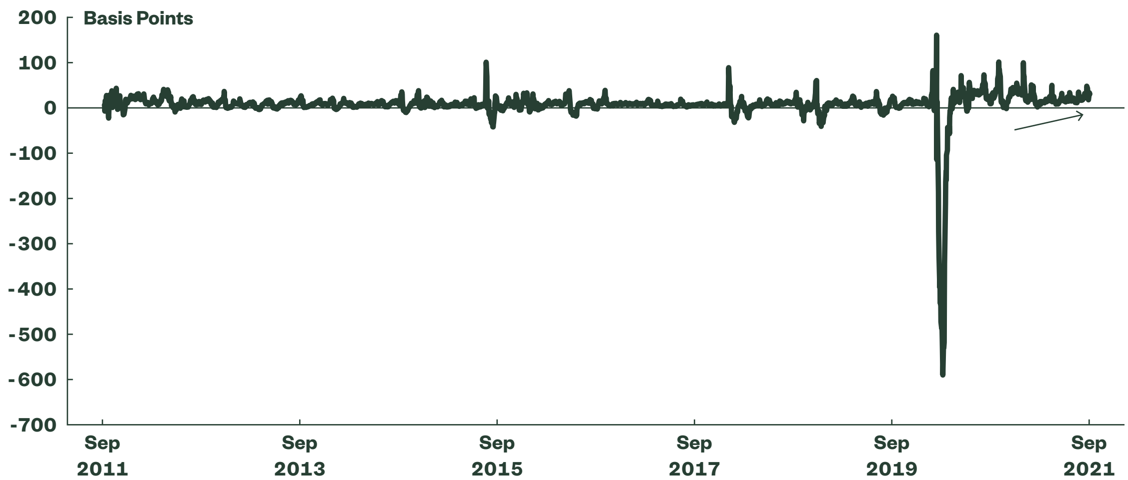
Readers who have made it this far into our Forecasts publication should be aware that our economics team has framed the backdrop as one of still-strong economic activity, but with the caveat that the global economy is working through an environment whereby growth, inflation and policy supports are in the process of peaking for this cycle. In mathematical terms, perhaps we are somewhere in the vicinity of an inflection point where the expansion endures but at a somewhat slower pace than the past year. And with an expectation of global growth surpassing 4% in 2022, surely the level of nominal sales swirling about the economy would be enough to bolster the share prices of listed firms replete with operating leverage.

Our perspective on financial markets parallels the economic baseline, even though the experience of markets doesn't necessarily mirror what occurs in the real economy. But we continue to see a healthy outlook for growth-oriented asset classes, albeit less so than in the recent past. Broad measures of sentiment and risk indicators still look reasonable, even if they are not landing in what we would consider a sweet spot for multiple expansion. Some of our business cycle indicators have decelerated but are not flashing any particular warning signs. Our expected returns for fixed income have come down but remain positive, and we continue to see a favorable environment for commodities even as certain assets appear extended. Overall, we retain an overweight allocation to stocks and commodities but have tightened the reins on the size of those positions given some degradation in our expected returns across asset classes.

Normal Readings from Risk Indicators

From the perspective of financial markets, the future is a scary place. After all, there is always something to worry about. And as the world continues to battle COVID variants, markets fret over the potential for higher interest rates and China balances capitalism with control, the present day is no exception. This is one reason why the variance risk premium (VRP) is typically positive — future (implied) volatility is generally a little bit higher than the trailing volatility recently exhibited by equity markets. A graphic of the VRP can be seen in Figure 5. What is most pronounced is that this indicator really starts to move during crisis episodes, and, to be clear, that is not what we are witnessing today. However, at the margin it has been ticking higher — gradually dimming our equity expectations in the process.

Figure 5
Variance Risk Premium



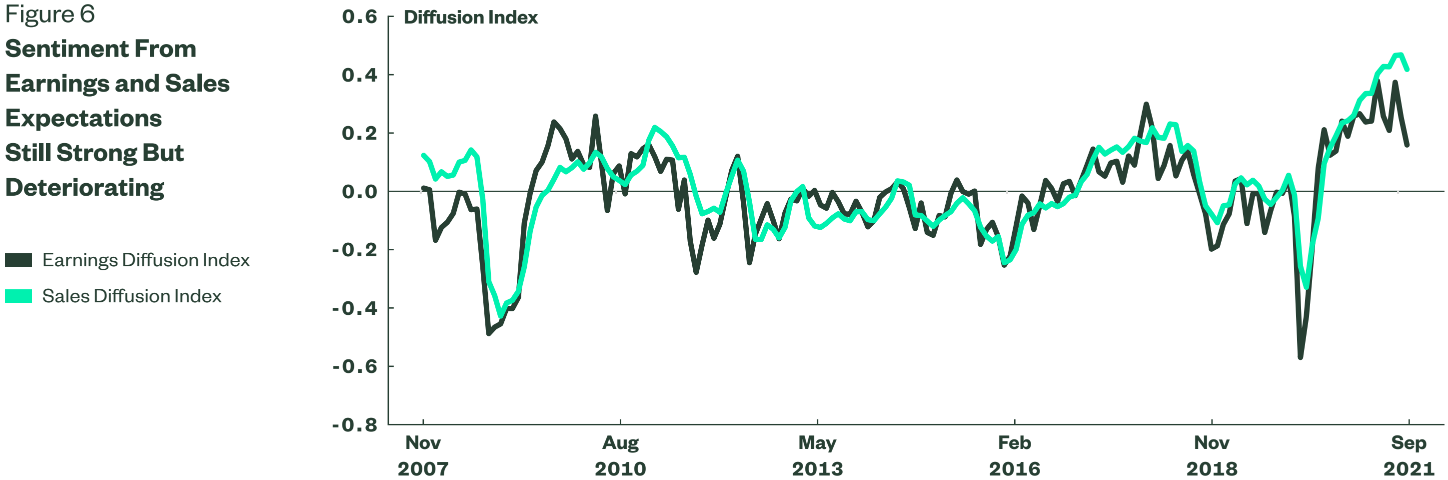
Source: State Street Global Advisors Investment Solutions Group as of September 30, 2021. Past performance is not a reliable indicator of future performance.

Our cross-asset risk gauge, the Market Regime Indicator (MRI), similarly is not flagging any serious risks or impending calamities. But it has also shifted out of a low risk aversion regime, which usually corresponds to a favorable environment for growth assets and currently sits in what we consider to be a normal regime. All else being equal, this means a lessened exposure to equities in our tactical asset allocation portfolios. In the economic jargon we discussed earlier, the MRI is likely past its peak but still in a decent spot as it relates to the outlook for equity markets.

Equity Earnings Expectations Increasingly Diffuse

Moving away from broader risk and sentiment indicators, there are other aspects of our equity research that are also pointing to a good, but perhaps not great, environment in the near term. Take expectations for sales and earnings as one example. In Figure 6, we show diffusion indices for both sales and earnings estimates for global equities. These indices are constructed such that if every earnings revision made were an upgrade then the value would rest at +1, and conversely if every revision were a downgrade the diffusion index would sit at -1. As can be seen, the levels of these indicators are still quite firm but earnings expectations have meaningfully decelerated and sales expectations have also started to roll over.

Figure 6
Sentiment From Earnings and Sales Expectations Still Strong But Deteriorating



Source: State Street Global Advisors Investment Solutions Group as of September 30, 2021. Past performance is not a reliable indicator of future performance.

Macro cycle indicators can take on a variety of shapes and sizes. If we consider a relatively simple construct using purchasing manager indices alongside the rate of inflation we will see another example where conditions are not quite as ripe as in recent months. Purchasing manager indices continue to point to strong and growing levels of activity, but at a less ebullient pace than was witnessed earlier in the year. And with inflation still elevated this has led our cycle indicator to shift from a boom period into a slowdown. In isolation, the combination of an easing in manufacturing growth and lofty price levels might suggest allocations to sectors of the market such as energy or health care. However, this insight from cyclical activity is but one part of a broader assessment. Energy also suffers from relatively weak expectations surrounding sales and earnings, as well as below average quality metrics. The same goes for health care, which also looks a bit expensive in our view. Instead, our sector investments favor technology and communication services, which rate most favorably from a sentiment perspective, and also the odd bedfellows of materials and consumer staples. Materials find support in their valuations and consumer staples look solid across all factors bar momentum.

From a regional equity perspective, one area where the investment climate has shifted more forcefully away from a mere deceleration would be in emerging markets, and China more specifically. This has been reflected in market performance as most equity markets were able to hold the line with neutral results during the third quarter while the MSCI Emerging Markets Index fell 8% and MSCI China shed nearly one fifth of its value. While we do see some reasons for optimism across emerging markets, including medium-term expectations of a weaker US dollar and still-strong manufacturing activity, a number of supports have faded or have been overwhelmed by the persistent policy interventions in the Chinese business landscape. From edicts governing the tutoring sector to antitrust rules in technology, alongside assaults on the video game industry and deeper dives into casino gaming laws, not to mention outright bans on cryptocurrency transactions, there has been a lot for foreign investors to digest. In our portfolios, we reduced emerging markets exposure early in the quarter and currently carry a neutral allocation.

In other global equity market allocations, we prefer US and European equities and we hold an underweight allocation to Pacific equities. Pacific shares have actually shown some signs of life, led by Japan, which is in the throes of a leadership transition, but the overall region continues to be weighed down by relatively weak momentum, sentiment and macro drivers within our quantitative framework. And any possible upside risk from a more assertive LDP leader taking the helm seems to have passed, with Kishida Fumio slated to become the next prime minister. In the United States, we remain concerned about what we view as under-appreciated risks associated with higher corporate taxes. And while the Federal Reserve has tilted to the hawkish side in their most recent assessment of the economy, this shift is not unique to the United States as the larger surprise for markets was associated with late September deliberations from the Monetary Policy Committee (MPC) of the Bank of England. And with the exception of steep US valuations, both US and European markets exhibit favorable outlooks within the context of our modeling.

Can Bonds Break Even With That Term Premium?

So, if we are moving into an environment where growth is likely to decelerate to some extent, and equities are incrementally less attractive, might that mean bonds could be more in favor? If the price action from September is any guide, the answer is an unequivocal "no." While the sell-off across global rates didn't match the pace or scale of what transpired in early 2021, it was enough to negate any benefit received from the rally that unfolded in July and this left most bond sectors with returns right around zero for the past quarter.

Our outlook for fixed income markets is not as severe as the market's repricing from September, but our expectations for bond returns (not dissimilar to our views on equities) have also compressed. As a starting point, it makes sense to take a look at how bond investors are currently being compensated. Figure 7 breaks down the components of the 10-year US Treasury yield across two different dimensions: 1) term premium versus short rates; and 2) real yields versus breakeven rates for inflation. As illustrated in the charts, both lenses show the 10-year yield at around 1.5% at the end of the third quarter. Arguably, the market's attention has been focused on the breakdown on the left-hand side, whereby we can see that the term premium is effectively nil and the bulk of investor compensation is derived from just the expectations of where short-term interest rates will be.[1] On the surface, it does not seem to be a winning proposition to assume 10 years' worth of interest rate risk without any accompanying term premium — until one realizes that this estimate of term premium has hovered in negative territory for the better part of the past three years. The chart on the right hand side decomposes the 10-year yield between inflation expectations (breakevens) and real yields. Here again, the forward-looking prospects do not appear to be bright with investors expected to sacrifice the purchasing power of their government bond investments. Unfortunately, this too has become a somewhat common feature of present day bond markets.

Figure 7a
Yield Decomposition

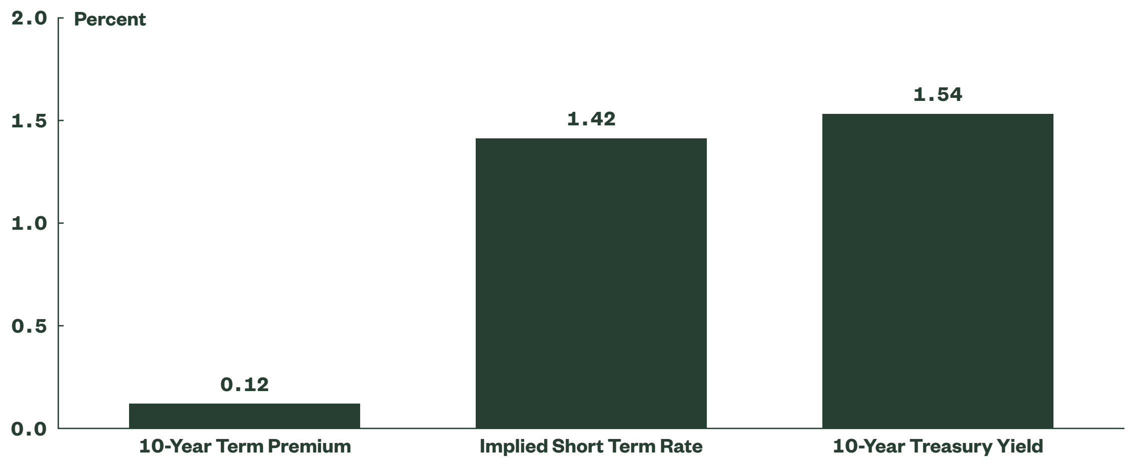
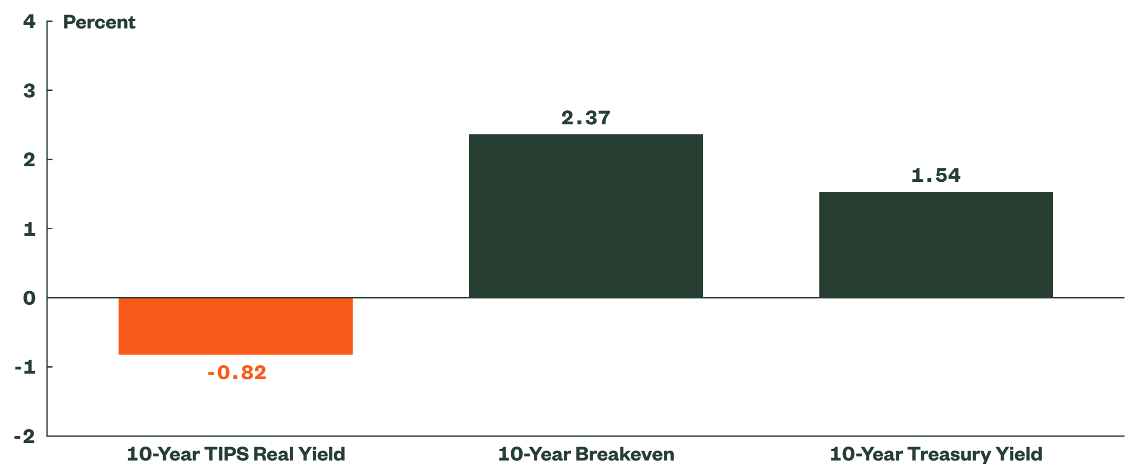


Figure 7b



Source: State Street Global Advisors, FactSet, as of September 30, 2021.

At the end of the day, even a $4 trillion dollar asset manager is just a price-taker in global bond markets, so we'll assess the opportunities as they present themselves. In our evaluation, those opportunities are mixed. While inflation patterns and shorter-term momentum had been promoting a view of lower interest rates earlier in the third quarter, those drivers have shifted and now look for steady to slightly higher levels of interest rates in the near term. Our yield curve modeling had been anticipating meaningful curve flattening amidst strong levels of economic activity and elevated inflation expectations. And while those conditions largely still hold, they have moderated as has our curve expectations and our forecasted returns for longer duration assets.

Backwardation and BTUs

Perhaps nowhere is the impact of supply disruptions more evident than in commodity markets — particularly for energy. From the consumer point of view, the spike in natural gas prices in some countries may catalyze crisis-level government intervention. For investors, it has thus far been a boon. Consider Figure 8, which plots the price of natural gas in the US market and in the UK market. A few points are worth highlighting here. First, it shows us what we already know — that natural gas prices have surged over the past several months. But these graphs also illustrate how much more severe the price moves have been in the UK — highlighting the very regional nature of certain energy commodities. The latest jump in natural gas prices in the US is hardly noticeable when contrasted against the rise that occurred in 2005 when supply was steadily falling (this was before the fracking boom), demand was steadily growing, and the country was hit by Hurricanes Rita and Katrina. Will natural gas prices remain elevated, or continue to rise? It's possible, but the factors driving this dislocation are varied and span warm weather in Asia to stagnant air flow in Europe. If the futures curve is any guide, it might be a while to get back to "normal" prices but investors probably shouldn't count on natural gas to lift broad-based commodity indices in the months ahead.

Figure 8a
US Natural Gas Prices

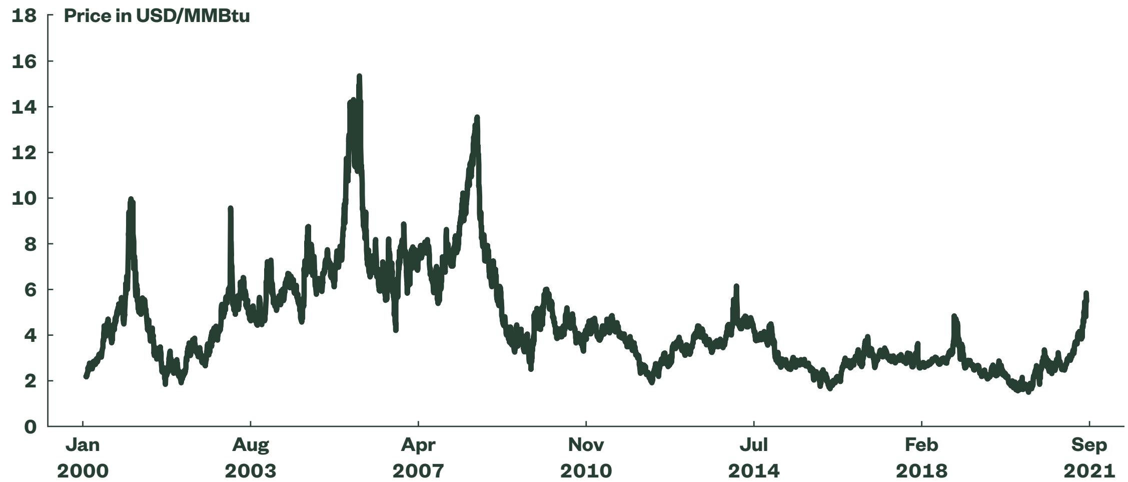
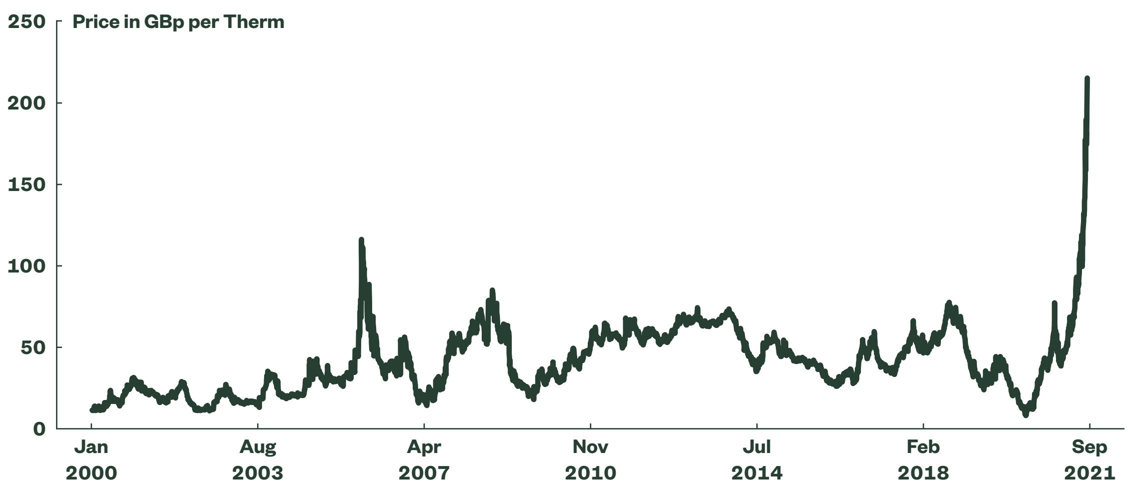


Figure 8b
UK Natural Gas Prices



Source: State Street Global Advisors, Bloomberg Finance L.P., as of September 30, 2021. Past performance is not a reliable indicator of future performance.

Elsewhere, our outlook for commodities remains broadly constructive. As China continues to manage the Evergrande fallout, growth-oriented commodities have rebounded from global growth and contagion fears, with surging demand highlighting the growing scarcity seen across physical markets, making many commodities increasingly vulnerable to supply disruptions and demand increases. OPEC continues to draw down global inventories through cautious production control, while disruptions from Hurricane Ida have moved US inventories to their tightest levels since 2018. Supply disruptions and robust demand for industrial metals have tightened fundamentals and continue to prop up their prices. Aluminum prices, which are already at decade highs, may continue to move higher as a military coup in Guinea threatens to shut down the country's supply chain of a key ingredient in aluminum production. All told, we continue to like commodities as we enter the final quarter of 2021, but like many other asset classes, some of the easier gains might just be behind us.

Sources: Bloomberg, FactSet, J.P. Morgan, Barclays, MSCI, Morgan Stanley and The Economist as of September 30, 2021.

Endnote

1 Market participants may conduct their own analysis and arrive at different term premium estimates. The data shown here uses the term premium as estimated by Adrian, Crump and Moench (ACM) of the Federal Reserve Bank of New York.

State Street Global Advisors Forecasts as of September 30, 2021

	2021 (%)	2022 (%)
Real GDP Growth		
Global	5.9	4.6
US	5.8	4.4
Australia	4.1	3.5
Canada	5.4	4.1
Eurozone	5.2	4.6
France	6.2	4.6
Germany	3.6	4.8
Italy	6.0	4.5
UK	7.0	5.6
Japan	2.6	3.0
Brazil	5.0	2.6
China	7.9	5.0
India	9.0	7.0
Mexico	6.0	3.5
South Africa	3.8	3.5
South Korea	4.0	3.0
Taiwan	6.2	3.0
Inflation		
Developed Economies	3.0	2.3
US	4.2	2.9
Australia	2.5	2.1
Canada	3.1	2.1
Eurozone	2.3	1.8
France	1.7	1.5
Germany	2.9	1.6
Italy	1.5	1.3
UK	2.2	2.8
Japan	-0.1	0.5
China	1.3	2.3

	September 30, 2021 (%)	September 30, 2022 (%)
Central Bank Rates		
US (upper bound)	0.25	0.50
Australia	0.10	0.10
Canada	0.25	0.50
Euro	0.00	0.00
UK	0.10	0.50
Japan	-0.10	-0.10
Brazil	6.25	8.75
China	4.35	4.35
India	4.00	5.50
Mexico	4.75	5.75
South Africa	3.50	4.50
South Korea	0.75	1.50
10-Year Bond Yields		
US	1.53	1.78
Australia	1.49	1.61
Canada	1.51	1.75
Germany	-0.19	-0.09
UK	0.95	1.26
Japan	0.07	0.14
Exchange Rates		
Australian Dollar (A$/$)	0.72	0.75
British Pound (£/$)	1.35	1.42
Canadian Dollar ($/C$)	1.27	1.24
Euro (€/$)	1.16	1.18
Japanese Yen ($/¥)	111.58	101.00
Swiss Franc ($/SFr)	0.93	0.99
Chinese Yuan ($/¥)	6.46	6.51

One-Year Return Forecasts	USD (%)	EUR (%)	GBP (%)	JPY (%)	AUD (%)	CAD (%)
S&P 500	6.2	4.4	1.0	-3.9	2.0	3.7
Russell 2000	6.5	4.7	1.3	-3.6	2.2	4.0
MSCI EAFE	5.7	3.9	0.5	-4.3	1.5	3.2
MSCI EM	7.8	6.0	2.5	-2.4	3.5	5.3
Barclays Capital Aggregate Bond Index	1.0	-0.7	-4.0	-8.6	-3.0	-1.4
Citigroup World Government Bond Index	-0.4	-2.1	-5.3	-9.8	-4.4	-2.8
Goldman Sachs Commodities Index	5.8	4.0	0.6	-4.2	1.6	3.3
Dow Jones US Select REIT Index	2.8	1.1	-2.3	-6.9	-1.3	0.4

State Street Global Advisors Forecasts as of September 30, 2021.
The above estimates based on certain assumptions and analysis made by State Street Global Advisors. There is no guarantee that the estimates will be achieved.

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Our clients are the world's governments, institutions and financial advisors. To help them achieve their financial goals we live our guiding principles each and every day:

- Start with rigor
- Build from breadth
- Invest as stewards
- Invent the future

For four decades, these principles have helped us be the quiet power in a tumultuous investing world. Helping millions of people secure their financial futures. This takes each of our employees in 30 offices around the world, and a firm-wide conviction that we can always do it better. As a result, we are the world's fourth-largest asset manager* with US $3.90 trillion† under our care.

* Pensions & Investments Research Center, as of December 31, 2020.
† This figure is presented as of June 30, 2021 and includes approximately $63.59 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.

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Marketing communication.

Glossary

Basis Point One basis point is equal to one-hundredth of 1 percent, or 0.01%.

Capital Expenditure (Capex) refers to investment by a company to acquire or upgrade physical assets, such as a building, IT hardware or a new business.

Citigroup World Government Bond Index The WGBI is a widely used benchmark that currently comprises sovereign debt from over 20 countries, denominated in a variety of currencies.

Consumer Price Inflation (CPI) A widely used measure of inflation at the consumer level that helps to evaluate changes in cost of living.

Deflation A decrease in the general price level of goods and services over a given period.

Goldman Sachs Commodities Index GSCI is the first major investable commodity index and includes the most liquid commodity futures.

Gross Domestic Product (GDP) The monetary value of all the finished goods and services produced within a country's borders in a specific time period. Economic growth is typically expressed in terms of changes in GDP.

Group of Seven (G7) A group consisting of Canada, France, Germany, Italy, Japan, the United Kingdom and the United States.

MSCI EAFE Index An equities benchmark that captures large- and mid-cap representation across 22 developed market countries around the world, excluding the US and Canada.

MSCI Emerging Markets Index The MSCI Emerging Markets Index captures large and mid-cap representation across 23 emerging markets countries. With 834 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

MSCI World Index The MSCI World Index is a free-float weighted equity index. It includes about 1,600 stocks from developed world markets, and does not include emerging markets.

Organization of Petroleum Exporting Countries (OPEC) 13-member group of oil exporting nations founded to manage global supply and coordinate pricing.

Purchasing Managers' Index An indicator of the economic health of the manufacturing and services sectors compiled from a survey of purchasing executives.

Quantitative Easing (QE) An extraordinary monetary policy measure in which a central bank buys government fixed-income securities to lower interest rates, encourage borrowing and stimulate economic activity.

Russell 2000 Index A benchmark that measures the performance of the small-capitalization segment of the US equity universe.

S&P 500 Total Return Index The benchmark that reflects returns after reinvestment of dividends of the 500 large cap stocks in the S&P 500 Index.

The US Dollar Index Measures the performance of the US Dollar against a basket of major currencies.

Yield Curve A graph or line that plots the yields of bonds with similar credit quality, typically from shortest to longest duration.

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