



Weekly Market Update

Global equities tumble on oil drop, China woes

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- U.S., European, and Chinese equity markets retreat as oil prices continue to drop.
- High-yield bonds also suffer, but U.S. Treasuries benefit from the “risk-off” environment.
- Consumer data ends 2015 on a mixed note, while manufacturing continues to struggle.
- While painful, the recent sell-off in equities has been orderly and controlled, contributing to our view that the decline is temporary.
- We strongly encourage investors not to be swayed by so-called “sell everything” rhetoric, and instead to take a long-term view.

January 15, 2016

Equities

Global equities extended losses from the prior week, with continued volatility in oil prices and fears of weakening global growth reverberating across markets. Despite a brief rally on January 14, the price of crude finished below \$30 per barrel on January 15.

In China, encouraging data showed rising exports and a surge in crude oil imports in December. Moreover, the country’s central bank steadied the Chinese currency, the yuan, during the week. Despite these positive signs, China’s main equity benchmark entered bear-market territory on January 15, having fallen more than 20% from its late December high.

Domestically, the S&P 500 Index added to its worst opening five-day stretch by losing 2.2% for the week. The index is down about 12% from its May high. Europe’s STOXX 600 Index fell 3.4% for the week, its third weekly loss in a row. Since reaching a record close in mid-April, the index has fallen 20.3%. (STOXX 600 returns are in local currency terms.)

Current updates to the week’s market results are available [here](#).



Financial Services

Fixed income

U.S. Treasuries rallied during the week. Oil price pressures, the potential for further yuan depreciation, and poor performance by equities and other riskier assets fueled investor appetite for safe-haven assets. The yield on the bellwether 10-year Treasury note closed at 2.03% on January 15 after briefly dipping below 2% earlier in the day. (Yield and price move in opposite directions.) The week's soft economic releases also increased Treasury demand.

Among non-Treasury "spread sectors," mortgage-backed and asset-backed securities posted modest gains, while both high-yield and investment-grade corporate bonds realized negative returns.

Consumer data is mixed, while manufacturing continues to struggle

The past week's light menu of economic releases contained a few disappointing data reports. Among the releases:

- **First-time unemployment claims** rose by 7,000 to 284,000, and the less-volatile four-week moving average, considered a more accurate predictor of labor-market direction, ticked up by 3,000, to 278,750.
- After rising briskly in November, **U.S. retail sales** fell 0.1% in December, as falling prices at the pump have yet to lead to stronger spending in other areas.
- **The Empire State manufacturing index** declined sharply, hitting its lowest level since April 2009. This followed reports showing a contraction in U.S. manufacturing activity in November and December.
- **Small-business sentiment** edged up in December, as measured by the National Federation of Businesses Optimism Index. Confidence over future sales were tempered by increased pessimism about business conditions overall.
- **Consumer confidence** rose for the fourth consecutive month, to 93.3, according to January's preliminary reading of the University of Michigan index.

Outlook

In light of the year's painful start, some voices in the market have been calling for investors to sell their stocks in favor of high-quality bonds. While such a strategy may offer surface appeal during periods of unsettling volatility in equity markets, we recommend taking a long-term view. "All or nothing" calls have generally led to undesirable results, as correctly predicting market tops and bottoms is very difficult. In addition, extreme asset-price movements have often presented attractive buying opportunities.

Thus far, this sell-off has been orderly and controlled. The CBOE Volatility Index (also known as the VIX, or "fear index") is elevated but has not reached panic levels

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and debt markets are functioning well. All told, we still believe this stock market decline is temporary.

As for the global economy, we believe that softer-than-expected growth in developed markets stems from a sharp decrease in oil-patch investment, along with surprisingly lackluster global consumer spending, given what amounts to a roughly \$7 trillion “tax cut” for consumers through lower energy costs. Renewed concerns over terrorism may also have weighed on confidence and spending.

However, we don’t believe the global economic weakness is systemic. Although growth forecasts have been reduced, we still expect annual global growth of about 2% this year, supported by a healthy U.S. labor market and stronger wage growth. Overseas, European data releases have been supportive of better economic activity in the region. As for China, the yuan is weakening only against the dollar, not a broad basket of currencies. This suggests that Beijing is not engaging in a currency war, and that the Chinese economy is not nearing collapse.

In fixed-income markets, investors are grappling with concerns over liquidity and, in this turbulent time, the possibility that some new risks may emerge. For corporate bonds, the metals, mining, and energy sectors continue to be the hardest hit, as the market focuses on whether oil price weakness signals a global slowdown or excess supply. With the possibility that oil could stay below the \$30 threshold, we are reaching a point at which further damage to credit markets is less likely. At the same time, we don’t think sentiment has reached bottom yet.



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Foreign stock market returns are stated in U.S. dollars unless noted otherwise.

Please note that equity and fixed income investing involve risk.

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