Capital Markets Strategy
Essential inCights for the C-Suite

MUFG

Policy Note

While visibility remains low in the current environment, the preponderance of "tail risk" should be lower in 2023 than it was in 2022. We highlight below our thoughts on both downside and upside risks for the year ahead.

We have also re-attached our comprehensive 2023 outlook publication, ***The New Macro Supercycle,*** released a few days ago.

Key Risks to Watch in 2023

While we expect "sticky inflation" to remain a concern this year, the markets will increasingly shift their focus from the "rising inflation" concerns of 2022 to "recession risk" in 2023. While risk remains high and visibility low, the preponderance of "tail" risk should be lower in 2023 than it was in 2022.

Economic Risk

1. Stagflation across global economy
2. Deeper global & US recession than anticipated
3. "Sticky" inflation (i.e., wages, services, food)
4. China's COVID re-opening
5. Sharp downturn in US consumer spending

Market Risk

1. Fed "higher for longer" than expected; implications of CB QT policy
2. "Gap risk" for HY credit spreads to recession thresholds
3. Structural vulnerabilities in leverage loan market
4. Credit cycle turn (downgrades & defaults)
5. Commodity and energy price resurgence

The Russia-Ukraine crisis remains a key concern in 2023. However, we also expect the US-China relationship to reassert itself as the most important, and politically challenging, bilateral relationship of the 21st Century. The implications for global growth, trade, supply chains and corporate strategy are likely to be formidable on a multi-year basis.

(Geo) Political Risk

1. Asymmetric Russia-Ukraine escalation
2. US-China decoupling (Taiwan, semiconductors)
3. Transatlantic Alliance friction (trade, China, Ukraine)
4. Iran instability
5. US debt ceiling showdown

Corporate & Strategy Risk

1. 2023 earnings & margin pressure
2. Cyber-security breaches
3. Labor market shortages; wage pressure
4. Exposure to "regulatory activism"
5. Funding market volatility, repricing

2023 Upside Risks

While a more balanced global recovery is more likely to occur in 2024, the year ahead could exceed consensus expectations if geopolitical tensions moderate, disinflation accelerates and the Fed succeeds in engineering a "soft landing" for the US economy

Global Economy in 2023		Global Markets in 2023	
1	COVID recedes into rear-view mirror; China rebounds quickly	6	More complete supply side normalization (labor, supply chains)
2	Rapid & broad-based disinflation (goods, services, energy, food)	7	Corporate earnings resilience, capex acceleration
3	US consumer resilience (spending, savings, employment)	8	Global M&A resurgence
4	US avoids recession ("soft landing")	9	Goldilocks for credit markets (rates, spreads)
5	India, China & SE Asia drive EM growth resurgence	10	Declining dollar reduces pressure on global economy and markets

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