Stargazer
Asset Management

What to focus on in Global Macro for the week of June 20th, 2022

Central Banks

It was a big week for central banks. Yes, the Fed hiked an aggressive 75bps, but more importantly, given what has already been priced by markets, they indicated they would be unrelenting until they see inflation improve convincingly.

Powell indicated that financial conditions had indeed tightened, and that was "a good thing". He said, "interest rates, yield curve shape, credit spreads, and equities are going to tell us how restrictive we are and how successful we are likely to be in slowing inflation down'".

For now, at least, they are still looking for tighter financial conditions, rather than worrying about a poor growth outcome. There is still no Fed put in sight.

Globally, the SNB and the BoE tightened policy, while the BoJ held off again, willing to risk increased market instability in order to achieve escape velocity from their long-standing disinflationary problems.

In the meanwhile, the ECB had to call an emergency meeting regarding "fragmentation" in sovereign debt spreads, after its promise only a few days earlier to address the issue forcefully, was openly challenged by the markets.

The meeting didn't yield a fleshed-out plan, but markets now assume they will implement some kind of European version of "operation twist", by which, for example, they might sell German 10-years to buy Italian 10-years. It was enough to meaningfully knock down the spread for now.

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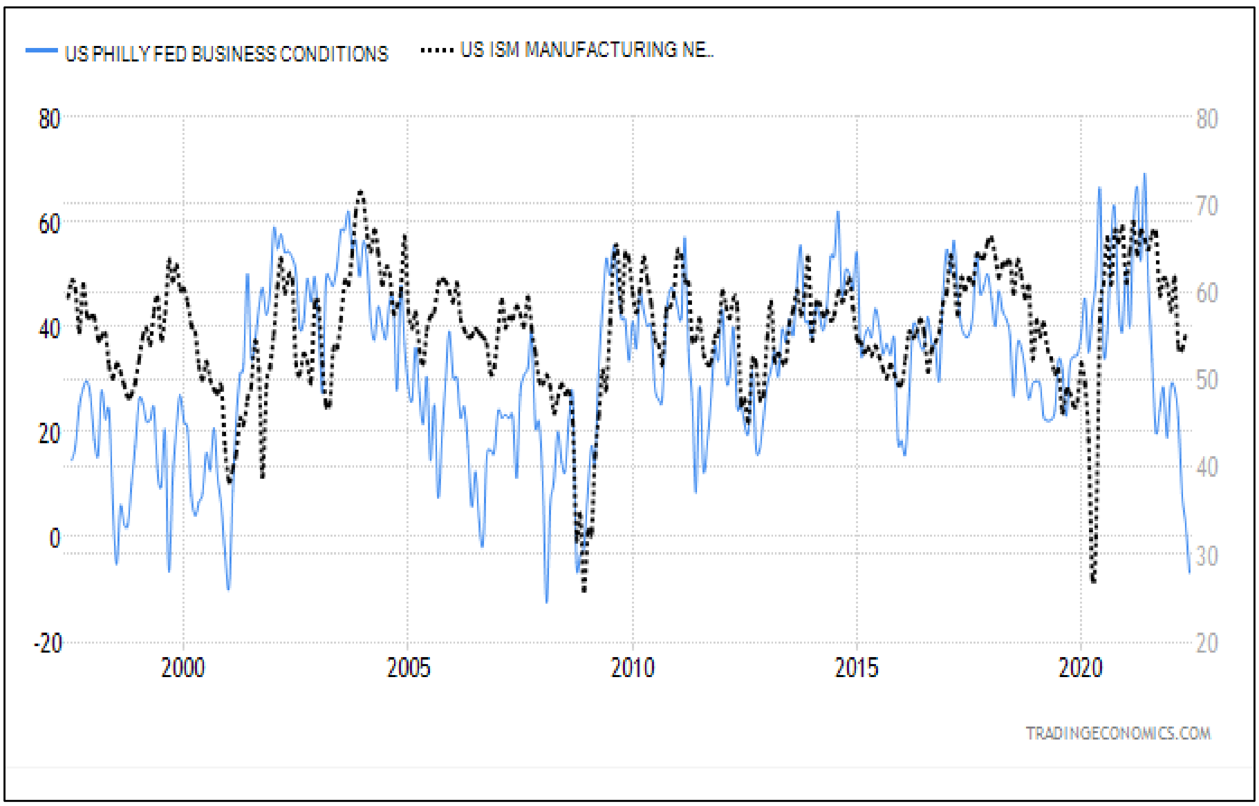
From inflation to growth fears…

While inflation is the main focus for central banks, growth is increasingly becoming the focus for markets.

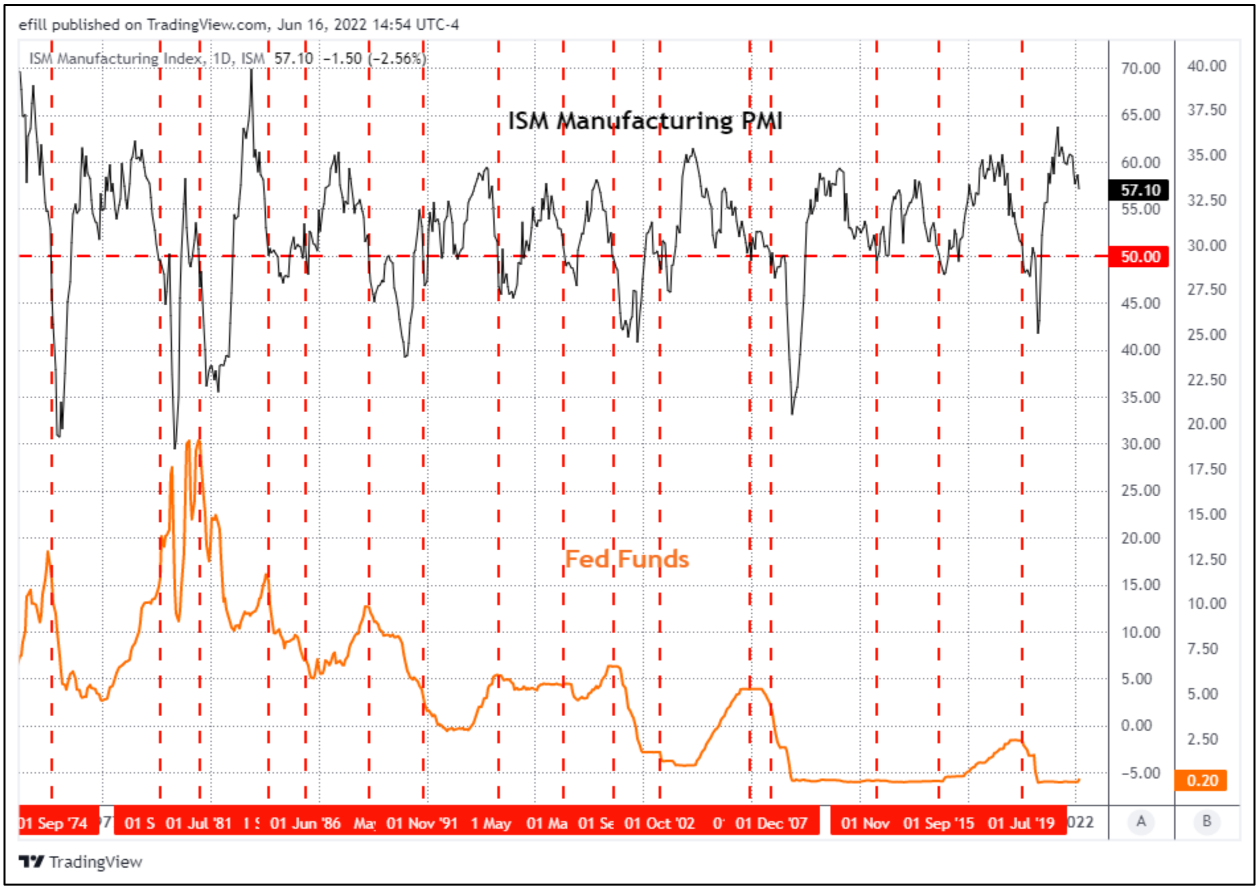
Last week, US retail sales posted the first drop this year as auto purchases led to a drop in consumption. Powell specifically mentioned retail sales as something they are watching closely given the large impact that consumption has on GDP.

The regional manufacturing surveys have been very weak recently. Last week's Philly Fed Survey reinforced that trend.

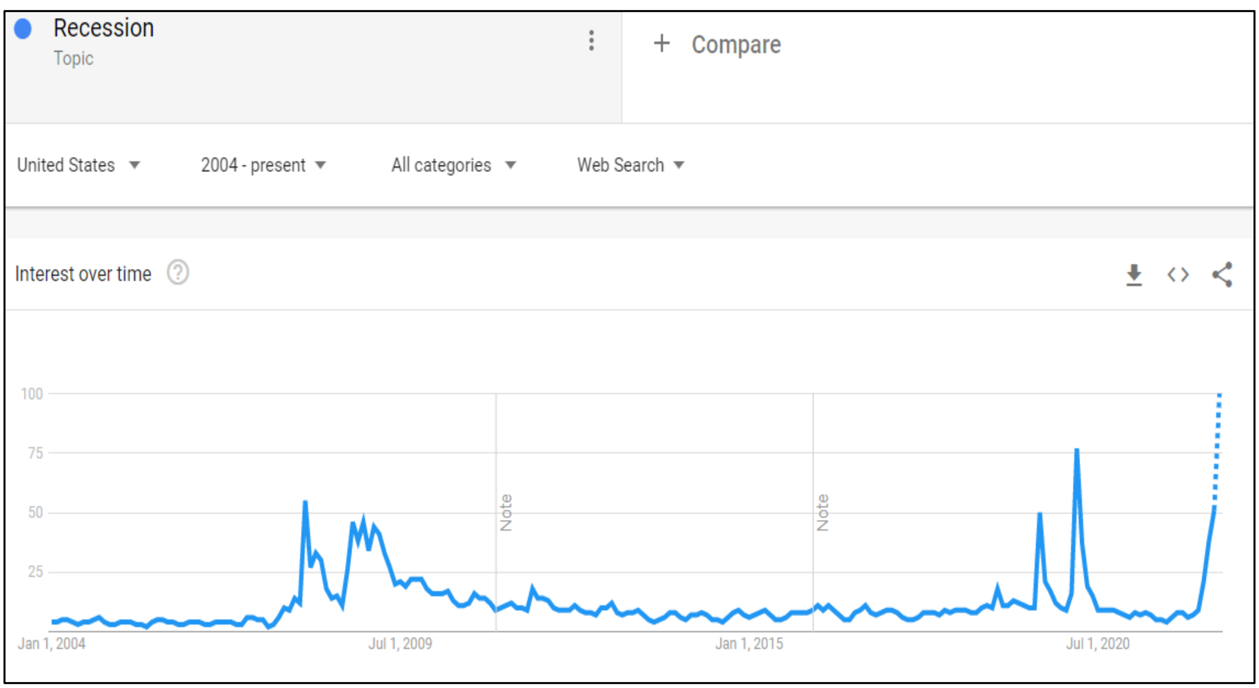
The last Philly Fed print is potentially pricing sub-50 in the coming months. In the last 50 years when the ISM falls through 50, the Fed has generally paused or cut rates. … how will the Fed react this time?



The one clear exception was in late '81, when Fed Funds continued to rise for a bit longer despite the ISM contraction. Given the Fed's current mood, that is of course a possibility.



Recession concerns are certainly on the rise. Google searches for the topic are seeing increased interest.



Fed tightening eventually breaks something. This time the threshold of what stops the tightening, at least given the Fed's current mindset, is more tied to inflation than growth.

The current combination of rising costs and falling consumption has small businesses worried.

Chart 10: Small business sentiment…

NFIB Small Business Sentiment

Source: BofA Global Investment Strategy, Bloomberg

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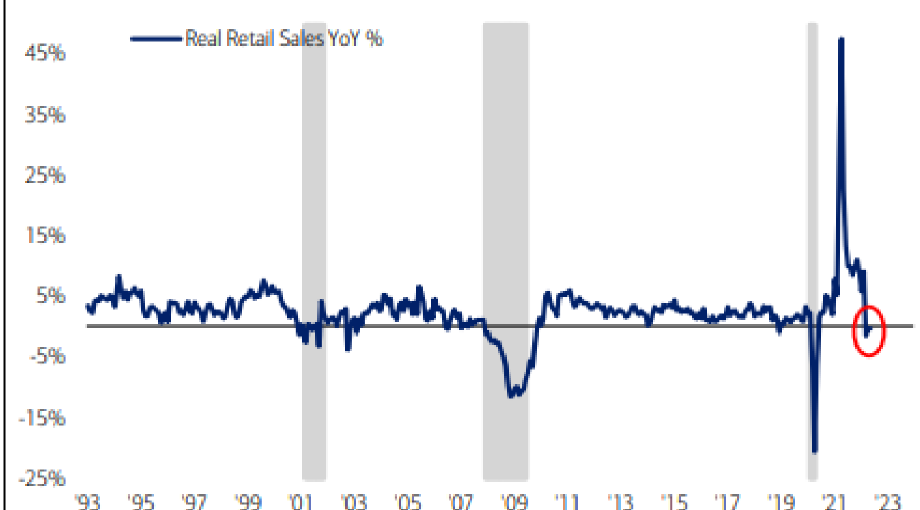
Real retail sales have dipped negative.

Chart 11: …and retail sales point to "recession shock"

Real Retail Sales YoY%



Source: BofA Global Investment Strategy, Bloomberg

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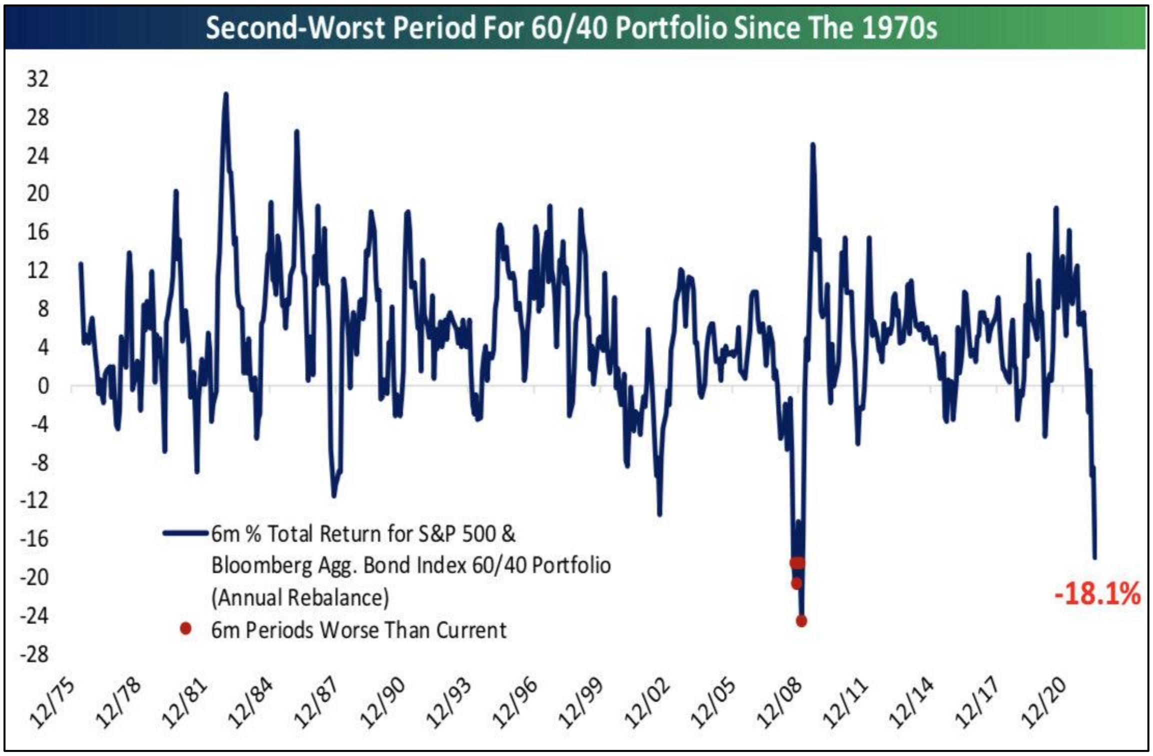
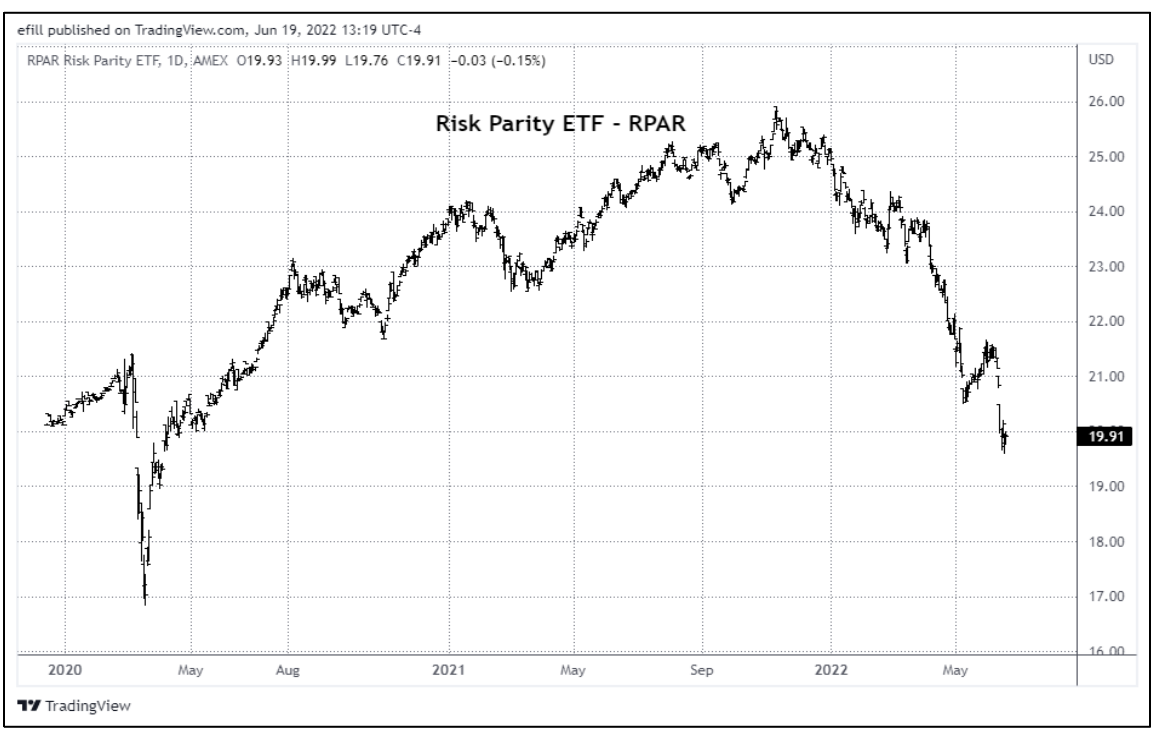
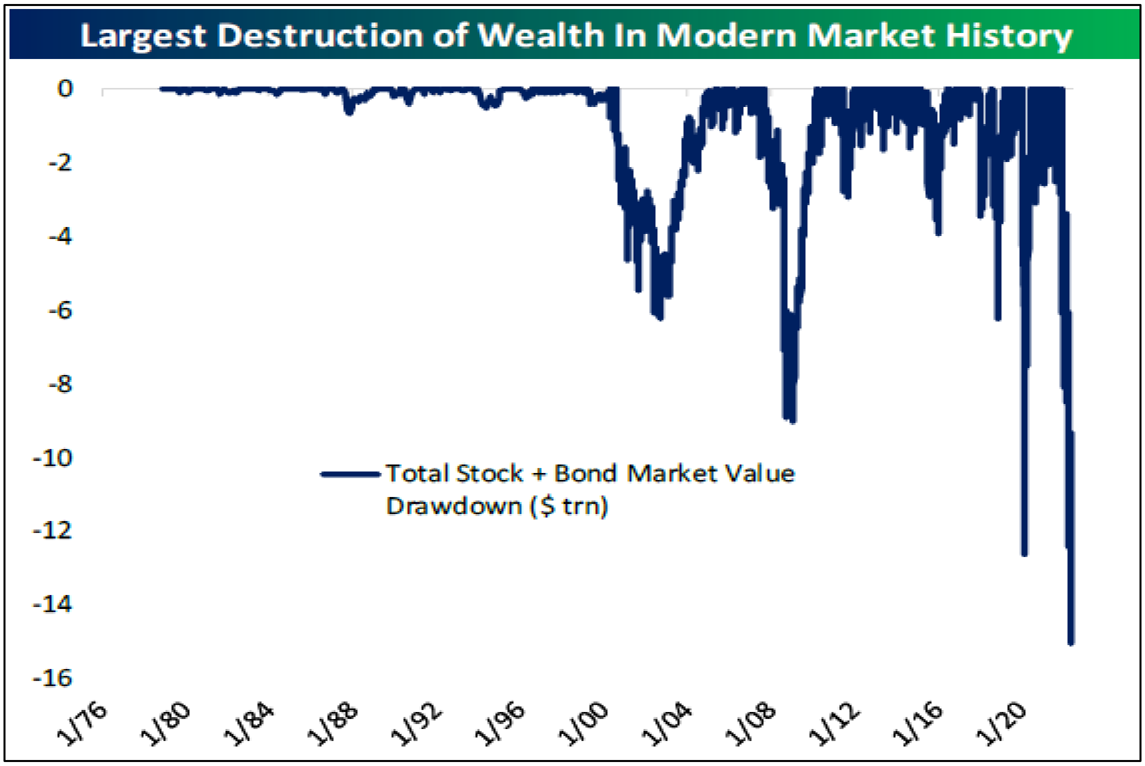
There may also be a wealth effect starting to kick in here. Most investors have little experience with a market where there are so few places to hide. With something like 90% of US investment capital said to have exposure that is similar to a 60/40 or risk parity portfolio, these are scary markets…





... and painful.



Source: Bespoke Investment Group

So, between stagflation fears and sagging markets, it is no surprise that sentiment is terrible.

Positioning and Flows

While the sentiment is certainly close to as bad as it gets, the picture in positioning and flows remains more confusing.

As of last week, global equity flows remained positive YTD.

Table 3: YTD flows into equities remain positive
Global flows by asset class, $mn

	Wk % AUM	YTD	YTD %AUM
Equities	0.1%	211,539	1.3%
ETFs	0.5%	328,616	4.4%
LO	-0.2%	-117,234	-1.3%
Bonds	-0.3%	-169,346	-2.4%
Commodities	0.0%	23,783	5.8%
Money-market	-0.7%	-269,469	-4.0%

*week of 6/15/2022. **Source:** EPFR Global

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Largely thanks to the US.

Table 4: Net fund flows to DM outpacing EM
Global equity flows by region

	Wk % AUM	YTD
Total Equities	**0.1%**	**211,539**
long-only funds	-0.2%	-117,234
ETFs	0.5%	328,616
Total EM	**0.1%**	**53,092**
Brazil	3.7%	350
Russia	0.0%	208
India	-0.8%	-2,170
China	0.6%	36,834
Total DM	**0.1%**	**158,447**
US	0.2%	135,550
Europe	-0.1%	-43,793
Japan	-0.2%	-4,674
International	0.0%	63,186

Total Equities = Total EM + Total DM
Source: EPFR Global

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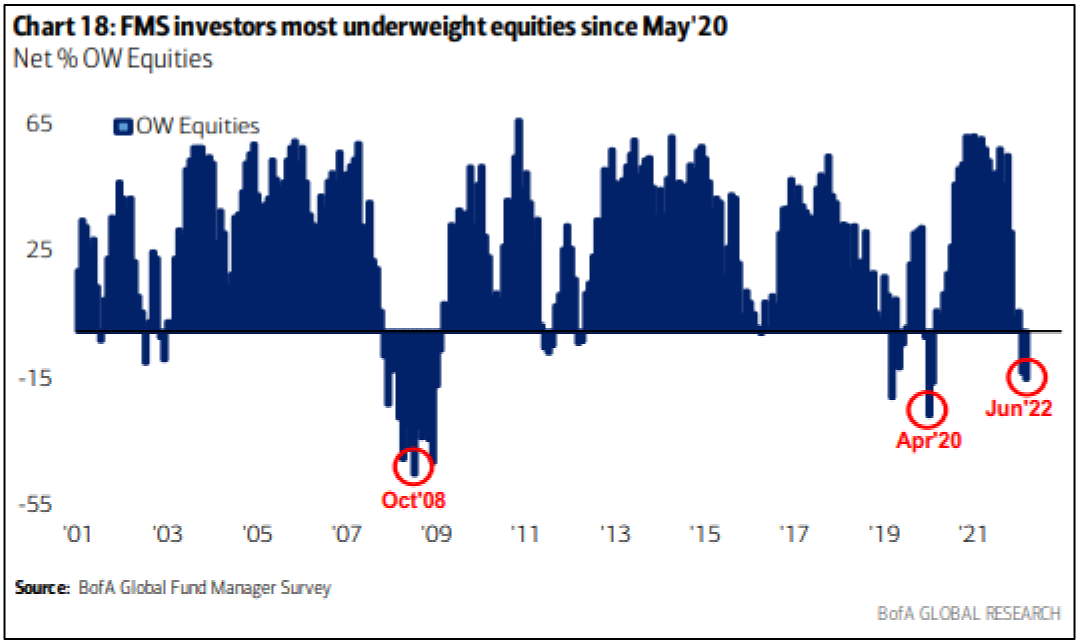
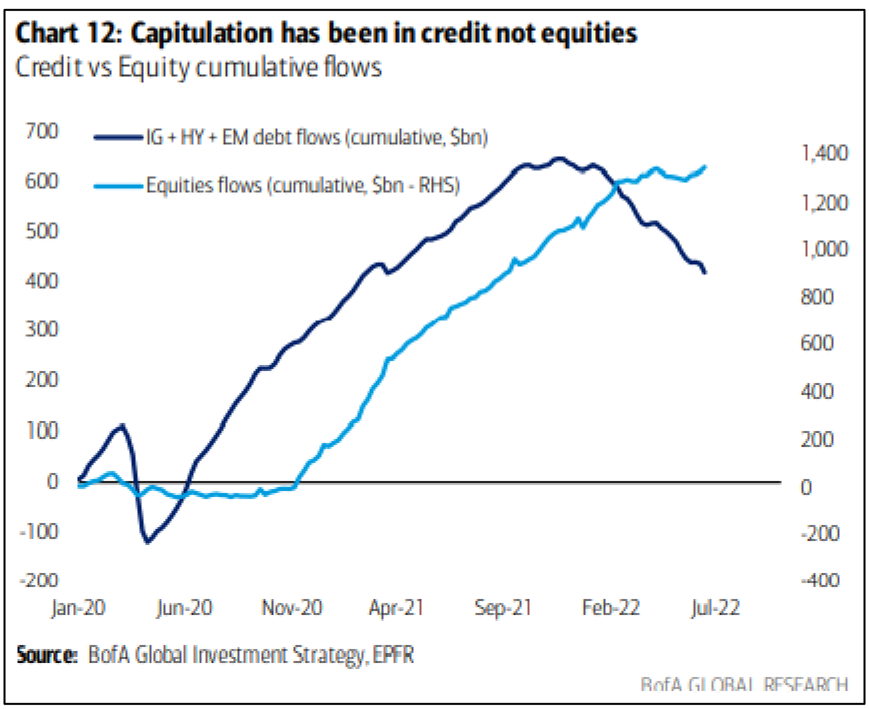
In fact, BoA reported net inflows into US equities of $16.6Bln last week. Yet, we apparently saw 90% of the stocks in the S&P decline in 5 of the last 7 days. I think there is a lot of confusion around data that is coming from different buckets, institutional vs. retail for example, and different markets, i.e. US vs. global.

Institutional investors seem now to be underweight.



However, global cumulative equity flows don't seem to have moved much.

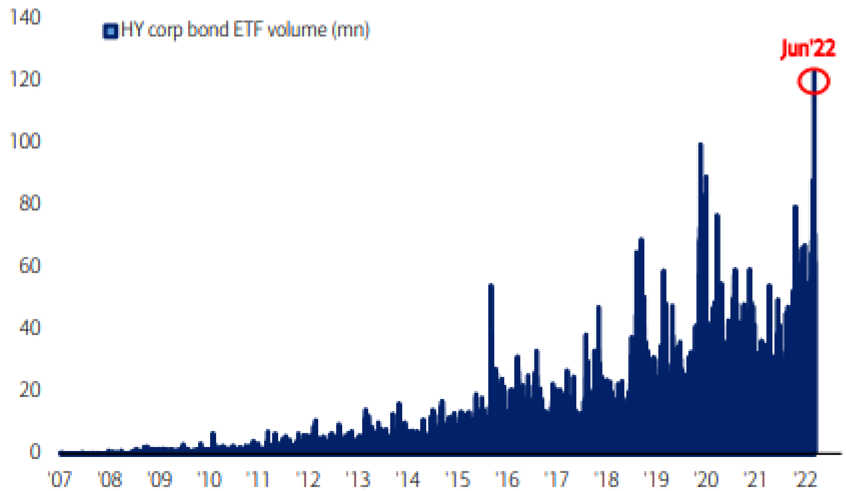
If anything, it is global fixed income that has taken the brunt of the selling, given inflation et al.



As BoA points out, the pinnacle of selling has been in credit recently, as we shift concern from inflation to stagflation.

HYG volume jumps as investors seek an exit a low liquidity market.

Chart 7: Capitulation...
HY corp bonod ETF (HGY) volume



Source: BofA Global Investment Strategy, Bloomberg
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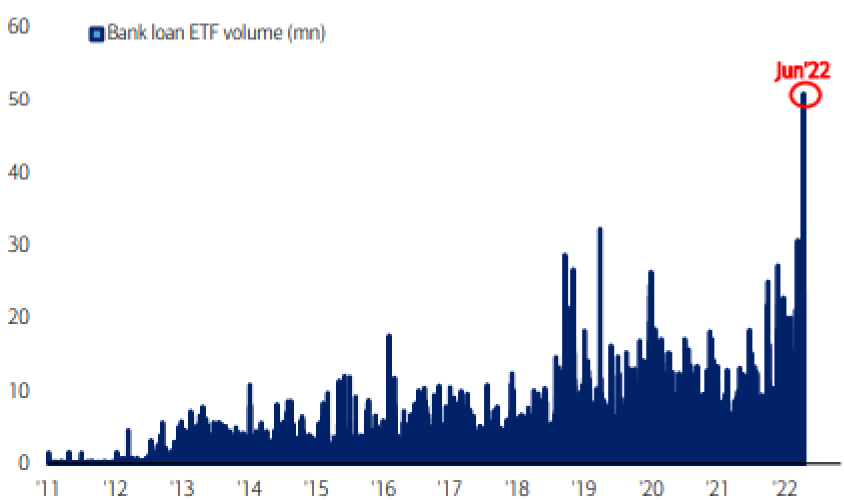
Even bank loans, with low duration, are seeing a rush for the exits.

Chart 8: ...has been in credit
Bank loan ETF (BKLN) volume



Source: BofA Global Investment Strategy, Bloomberg
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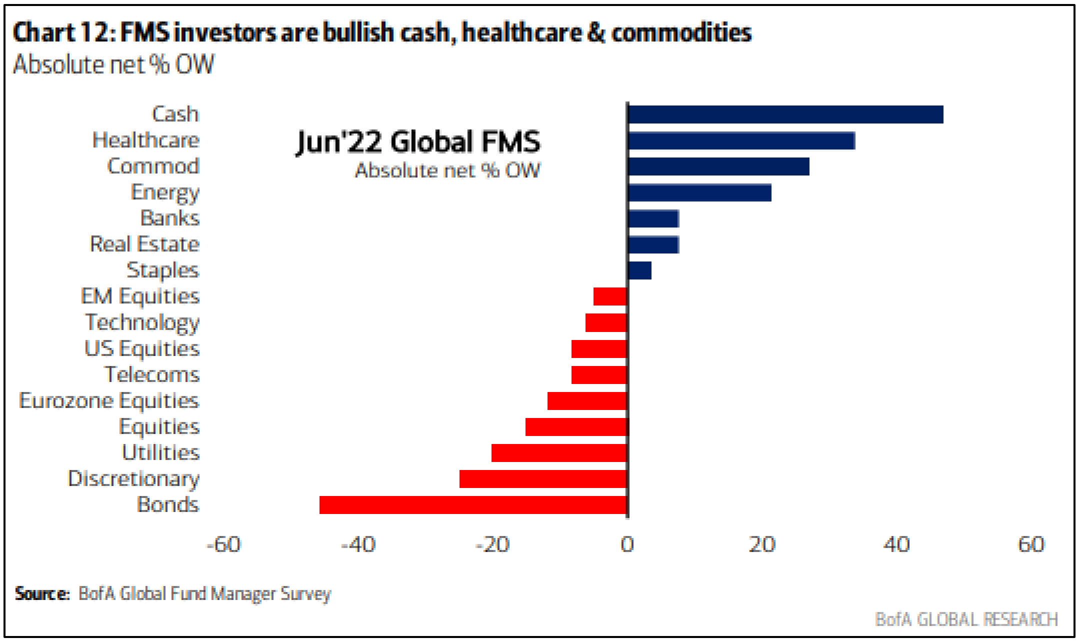
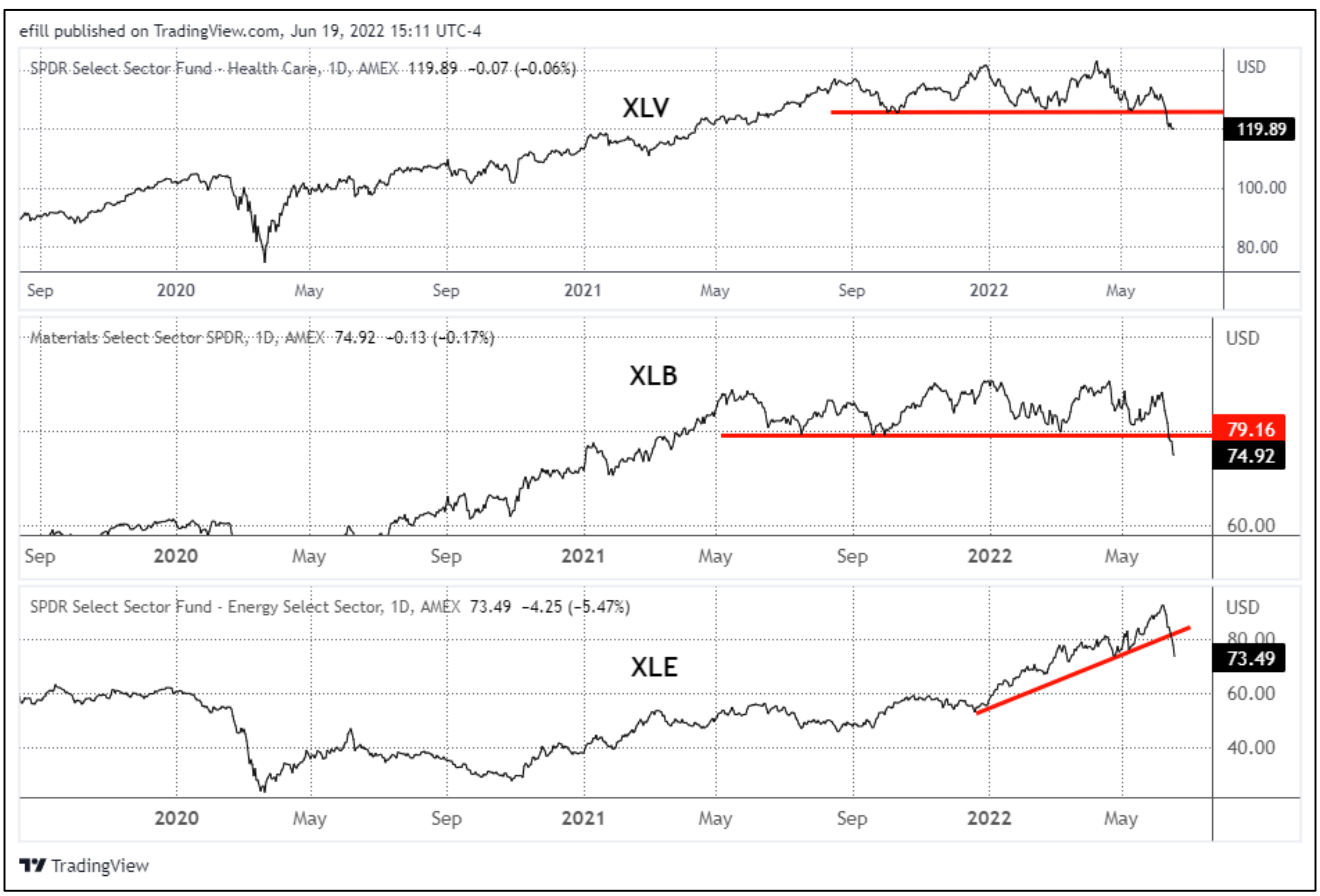
In equities, people have been hiding in healthcare, materials, and energy.

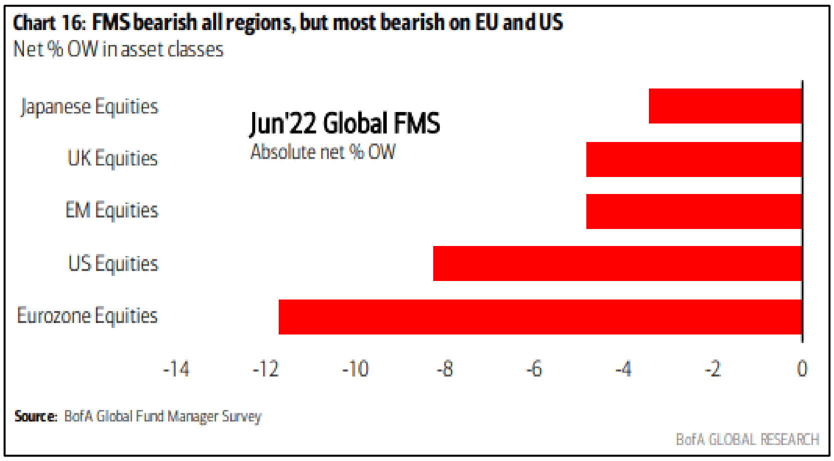


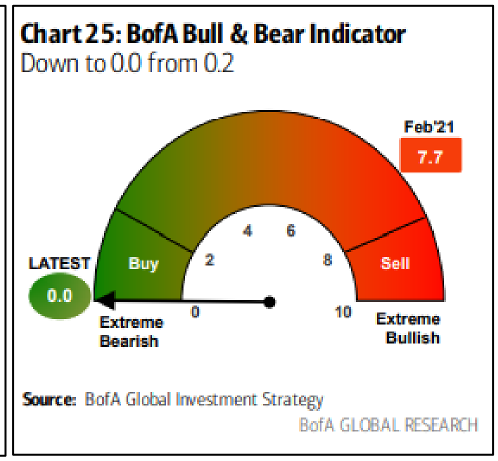
All three got hit hard last week.



In global terms, Europe and the US remain the most out of favor. If good were to come out of Ukraine, as some kind of a peace deal is reached, those two should do the best. They have the highest inflation and have the most to gain from a better geopolitical outcome.

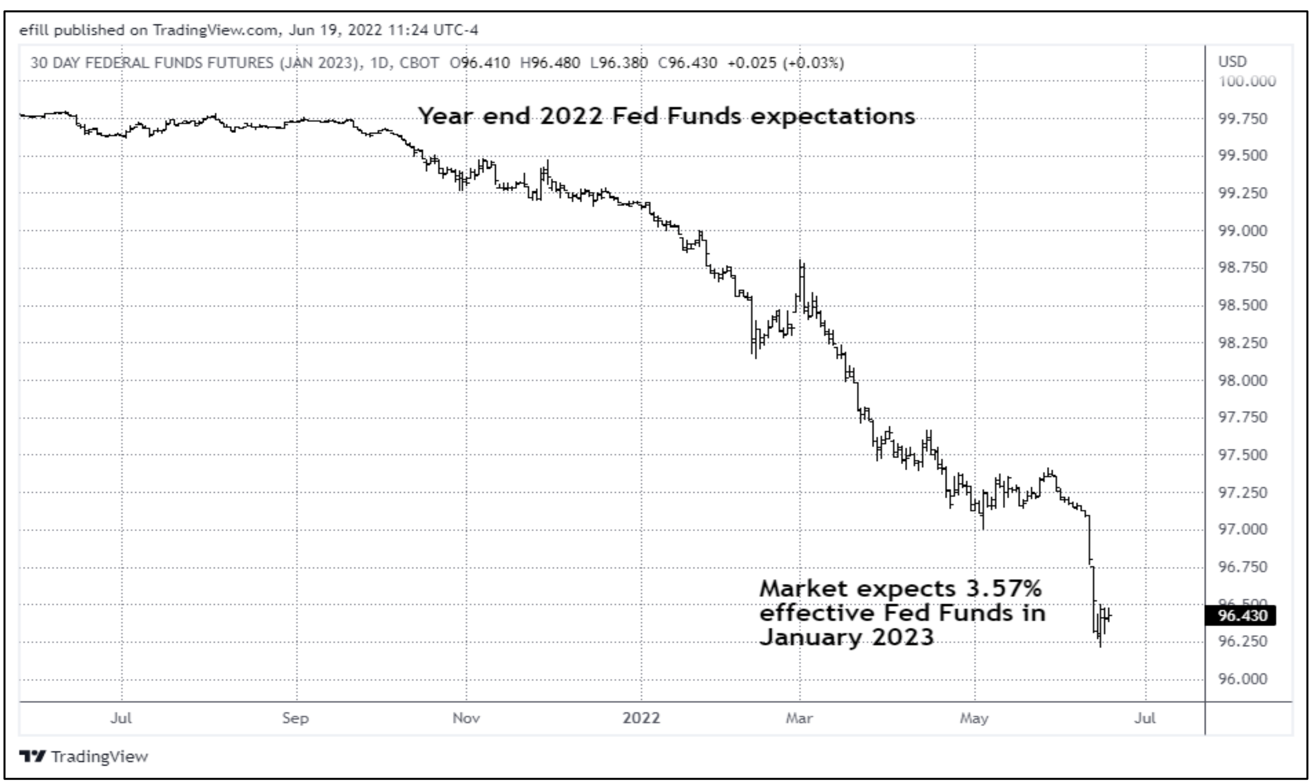
In the meantime, BoA's Bull & Bear indicator remains pinned at max fear.





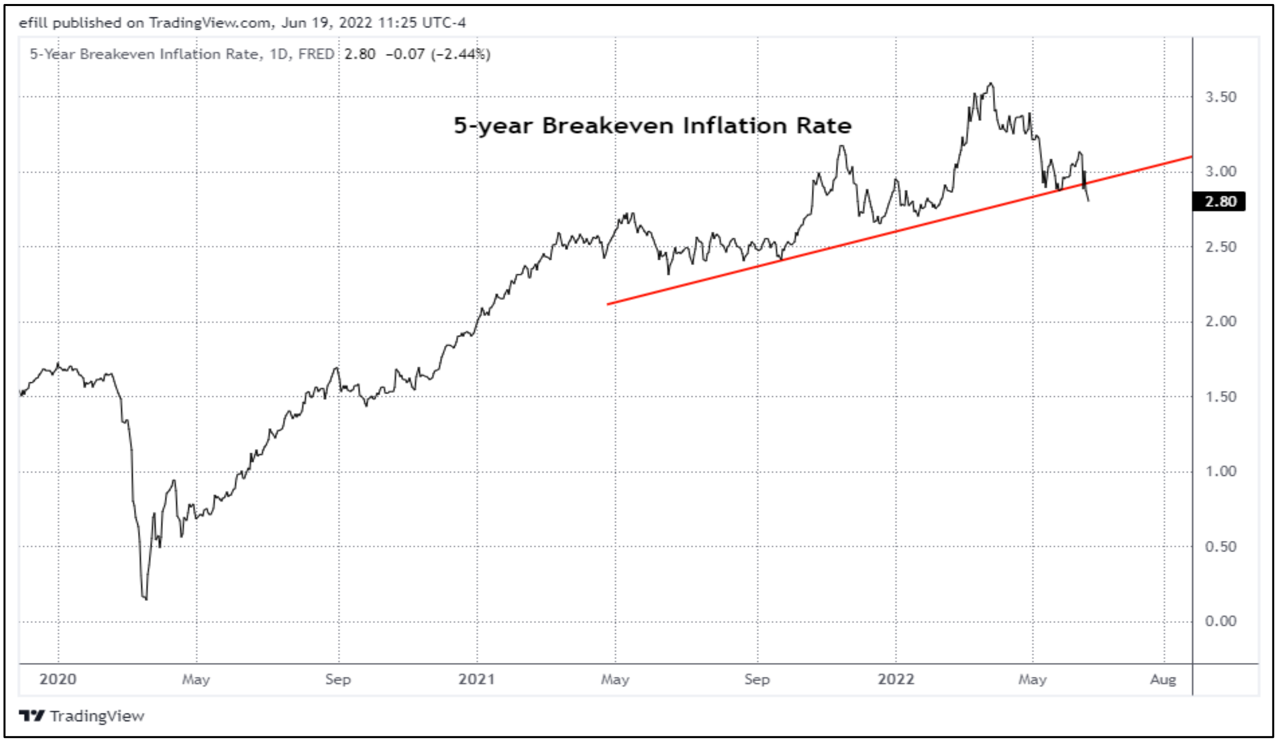
Interest Rates

Despite rising growth concerns, the market is still looking for Fed Funds to be well north of 3% by year-end.



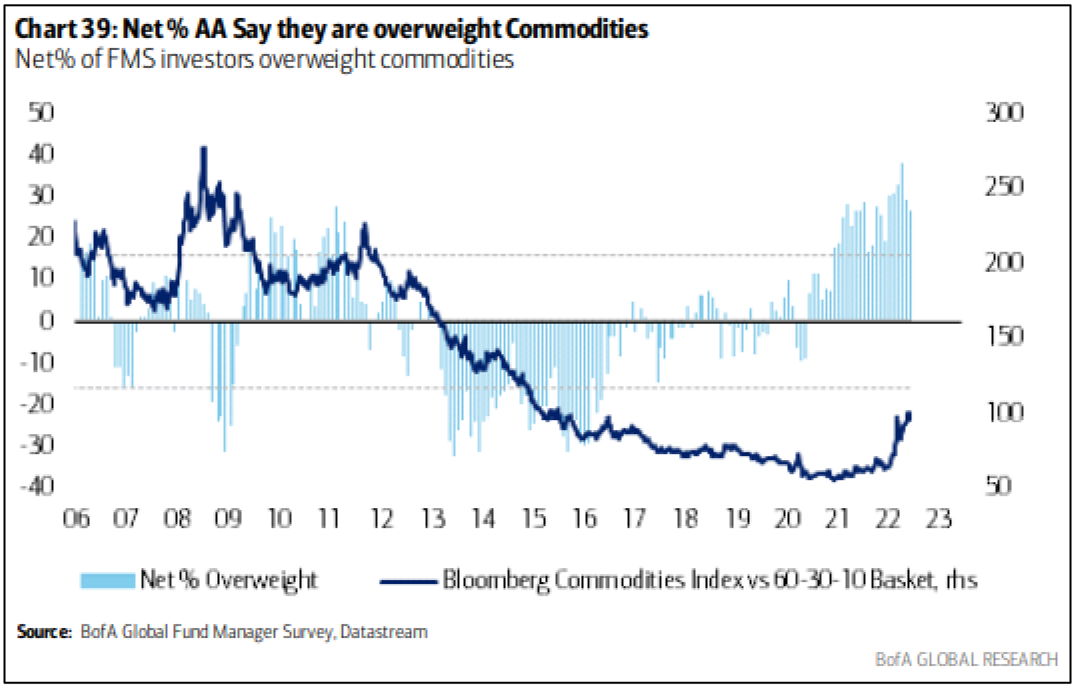
At the same time, the curve has continued to flatten, toying with inversion.

Last week's drop in oil prices took down breakevens as inflation expectations eased a bit.

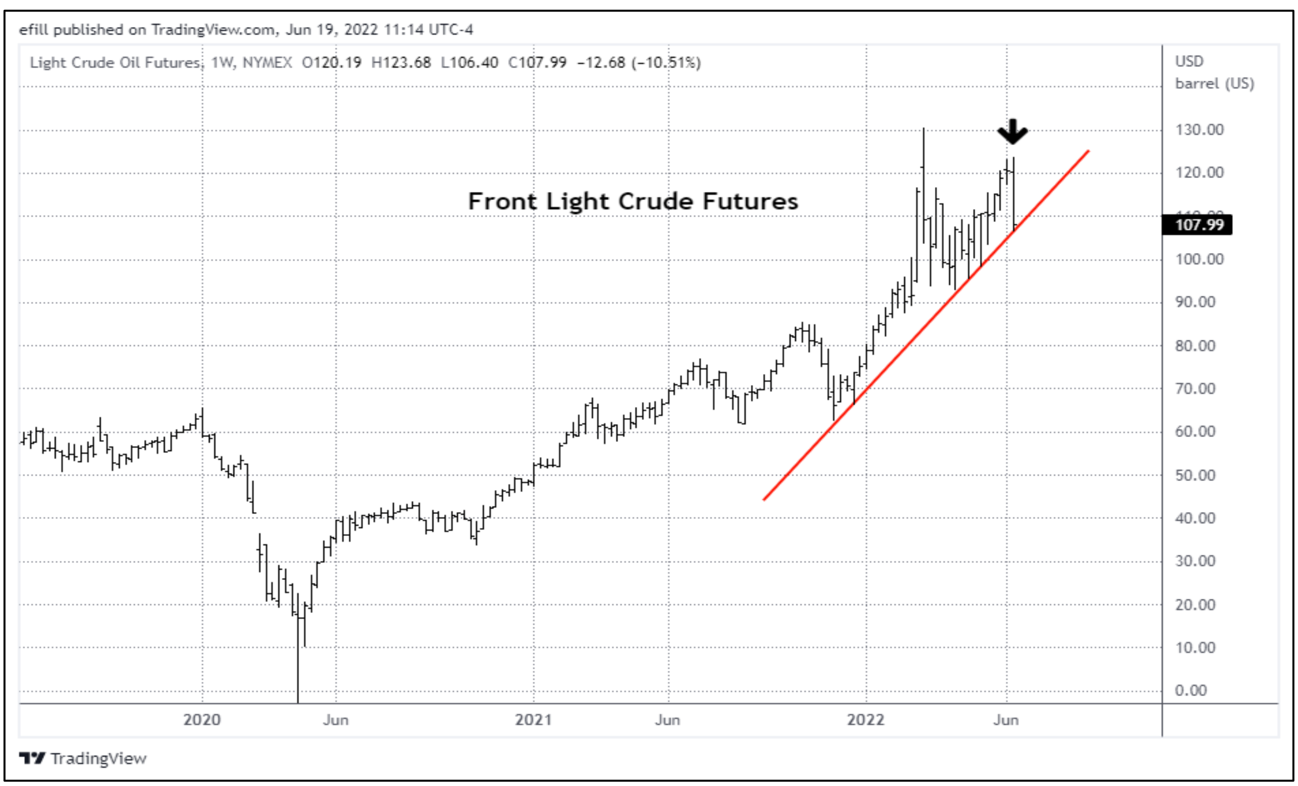


FX – The DXY belies some of the volatility we have seen related to CB moves in DM and risk-off/growth fears in EM and commodity-related currencies. Some, with reversals of reversals.

Commodities – Here too volatility has only picked up. The switch from a focus on inflation to global growth is making for some large reversals. Crowded longs in commodities is amplifying the moves.

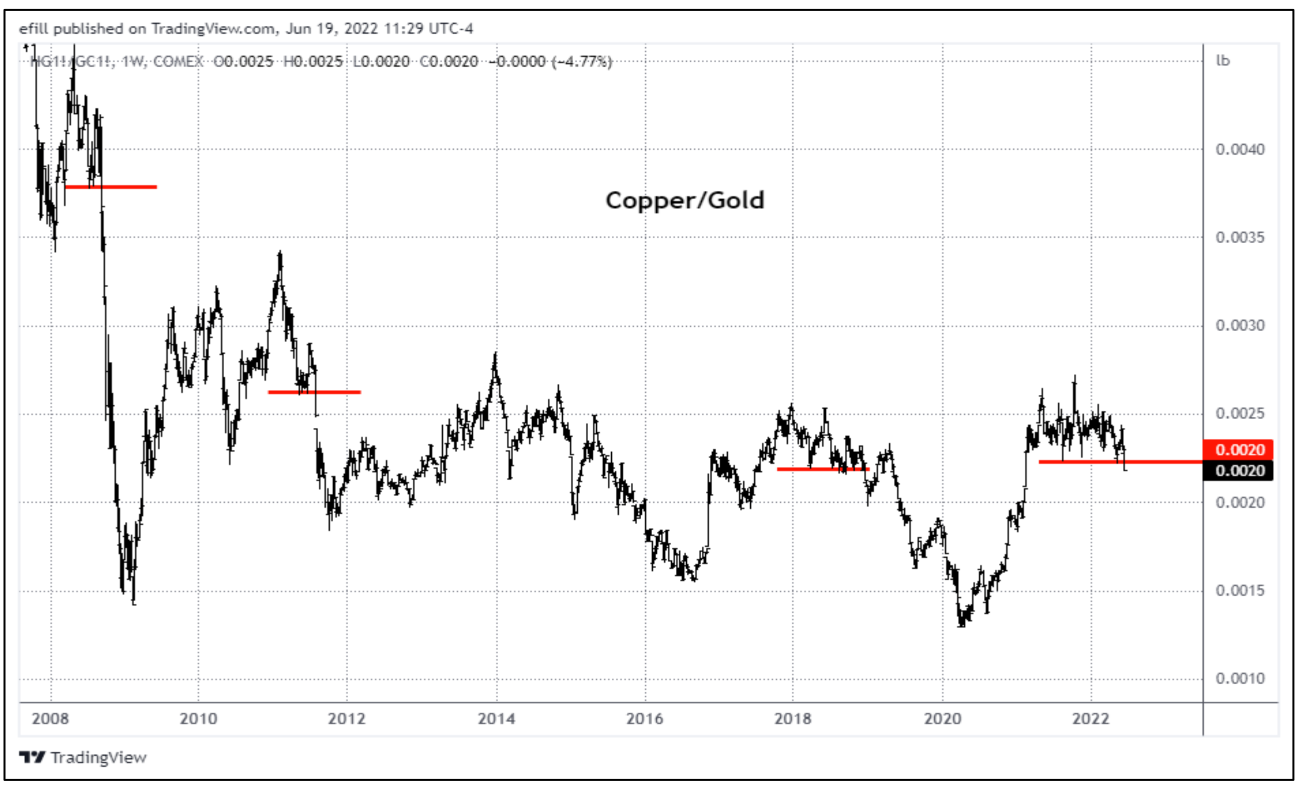


A brutal weak in energy produced an outside week down in oil futures.



Copper, in short supply, but very reactive to global growth, is again threatening to crack support.

Historically, a falling Copper/Gold ratio has meant lower bond yields and falling growth.



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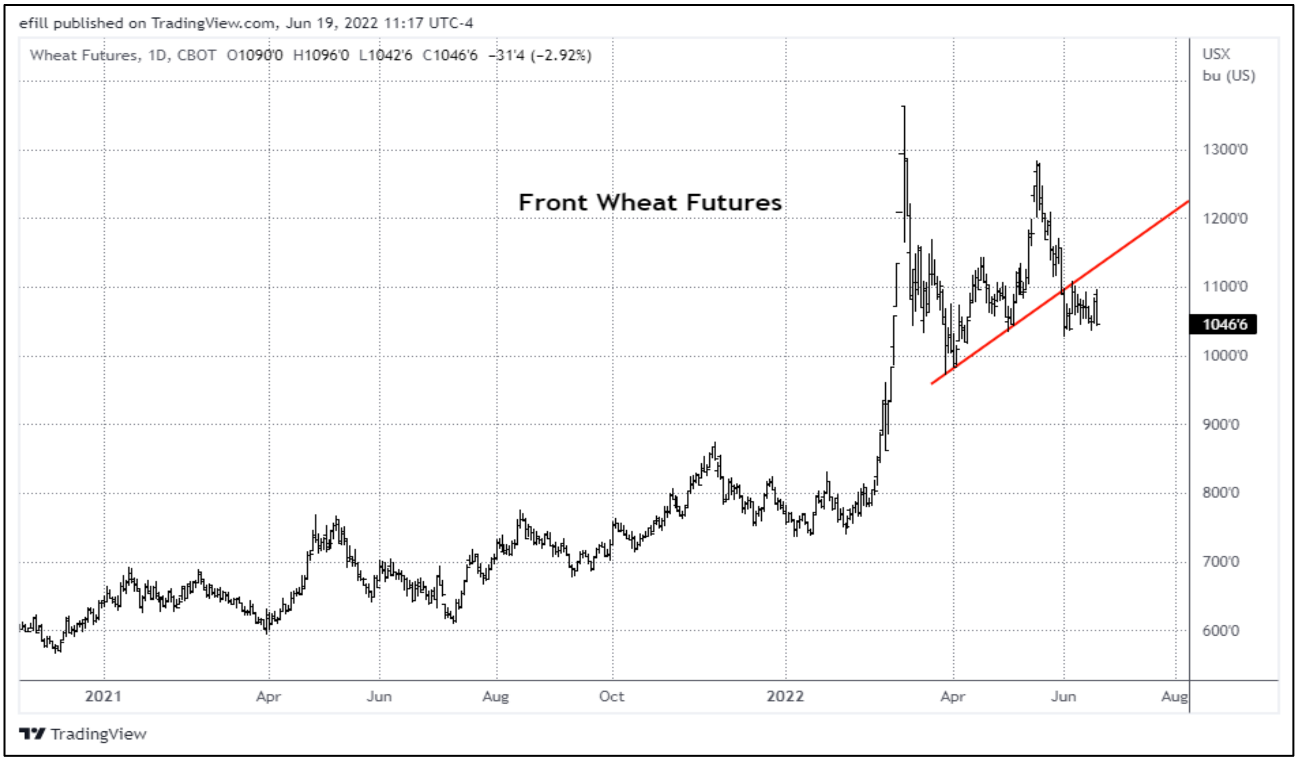
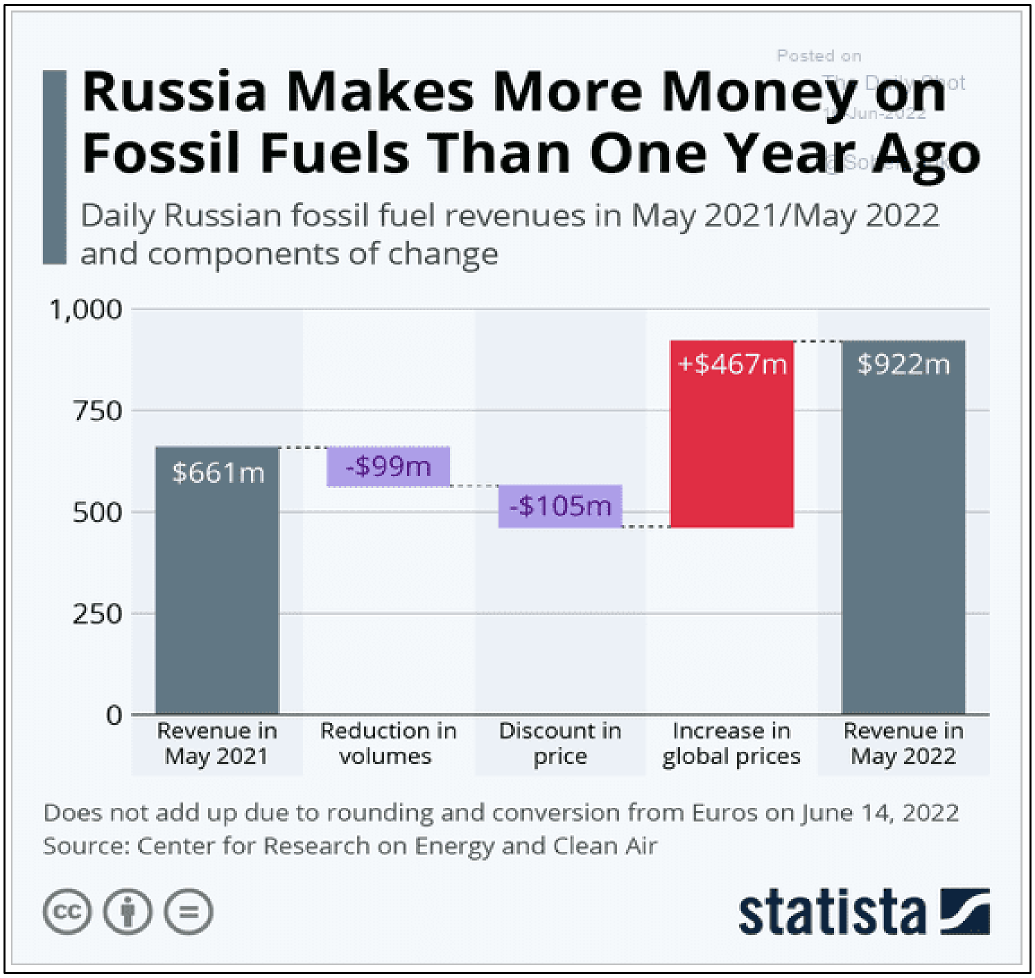
Even wheat has not been able to regain the uptrend.



Crypto reached my target. I don't have a near-term view now. At < 1/3 of its top tick market cap it probably matters less anyway. (That was my friend Brent Donnelly's idea, and I agree.)

Last one…



The shortened week for US markets brings Fed's Chair Powell testimony to Congress and global flash PMIs for June.

Important Macro Data Releases and Events for the Week

Monday 6/20/2022	PBoC Interest Rates Decision (Sunday night ET)
	Juneteenth Holiday
Tuesday 6/21/2022	Retail Sales (Apr)

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BoJ Monetary Policy Meeting Minutes

Wednesday
6/22/2022

CPI & PPI (May)

CPI (May)

Fed's Chair Powell Testifies

Consumer Confidence (Jun)

Manufacturing and Service PMIs (flash)(Jun)

EU Leaders Summit

Thursday
6/23/2022

S&P Global Manufacturing, Service, and Composite PMIs Europe & US (flash)(Jun)

Fed's Chair Powell Testifies

Initial Jobless Claims

Initial Jobless Claims 4-week average

Continuing Jobless Claims

EU Leaders Summit

CPI (May)

Friday
6/24/2022

Central Bank speeches from AUD and GBP

Michigan Consumer Sentiment Index (Jun)

New Home Sales (May)

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