Stargazer Asset Management

What to focus on in Global Macro for the week of November 9th, 2020

Macro Themes on the Radar:

Election

With the Electoral College results unlikely to be meaningfully impacted by Trumps impending legal challenges, the Presidential election looks to be over. Democrats had small losses in the House while Republicans look likely the hold a slim majority in the Senate.

As if the politics have not been interesting enough, Biden's choices now will determine what the next four years look like. So far, he has gone out of his way to emphasize that he will represent all Americans. With over 70m people voting for the other guy, he has his work cut out for him. How he chooses to populate his cabinet will make a strong first impression and will set the tone for his administration. There is a lot of focus on how much he owes to the "progressive" wing of the party and to what extent he will choose to, or be able to, keep his administration on the more centrist Obama/Clinton path. Who for instance will get Treasury? Will it be someone like Warren or like Bloomberg… the excitement isn't over yet.

Early on, Biden might do well to take a leaf from the Fed's "Fed Listens" initiative. During the series, regional Fed banks held conferences and townhalls around the country. These events sought to interact with a wide range of economic participants, including individuals and organizations, to understand how the country viewed labor market conditions, inflation and interest rates. Note that the initiative was completed before COVID struck. There is a lot in here worth perusing. For a quick overview, pages 6-8 provide a summary of findings. The report has almost certainly informed the Fed's current actions and outlook and is worth a look for that reason alone.

This type of initiative would be an interesting way for the new administration to begin the process of bridging the national divide. Understanding actual concerns, could be a path to enacting policies that stand the test of time rather than ones that are overturned by one side or the other every 4 to 8 years.

Fed and ECB

Last week's Fed meeting delivered no policy adjustments, only a slight downgrade to the assessment of the current situation. They gave no hints of what comes next other than that more fiscal support from the government is needed and that further monetary policy adjustments are possible.

This contrasts with the ECB Lagarde's comments two weeks ago that we should expect an adjustment to policy at the December meeting. Bloomberg points out that she referred to a "recalibration" of measures 20 times during her press conference. She made no mention of what the changes will look like. Instead, making it clear that everything is on the table for review.

This has analyst's speculating on what might be included in the coming package.

Here are the top candidates in order:

- A €500b increase in the Pandemic Emergency Purchase Program (PEPP) and a 6-month extension to the program.
- A doubling of the current Asset Purchase Program from €20b to €40b a month + the current boost of up to €120b. (this is more restrictive that what can be bought under PEPP with country capital keys et al)
- An expansion of the private debt buying program to include "fallen angels" that have had rating reduced to junk post the virus outbreak. They could also add bank debt to the list of approved debt for purchase, although some see that as a potential conflict of interest given the ECB's role as eurozone bank regulator.
- Augmentation of the TLTRO program of cheap financing for banks. Potential loosening of collateral requirements, better terms, etc.
- A further reduction in the deposit rate from the current -.50bps. This is seen unlikely by many because of its mixed results and the strain it puts on banks (could be counteracted by increasing exemptions and changes in TLTRO). I think they save this for a EUR protest if it gets too strong and "inhibits monetary policy transmission."
- Something unexpected that provides a jolt. Buying stocks?

What to Focus on Now:

A constantly shifting narrative…

Over the last few weeks, the "blue wave" had been increasingly priced by markets. However, it was quickly downgraded on Wednesday as the prospects of a split Congress lessened expectations for large near-term fiscal stimulus. Bond yields fell and the nascent outperformance by banks was quickly reversed as a result. Instead, we priced a higher reliance on the Fed to provide further liquidity as the burden shifted from fiscal back to monetary policy. This helped drive dollar weakness into the weekend, as endless liquidity provision is not only ensured, but might need to be increased to make up for a delay in fiscal stimulus.

Either way there is little chance that any reduction in fiscal or monetary stimulus is coming anytime soon. In fact, the opposite is likely, as COVID fears continue to bring renewed lockdowns and economic uncertainty.

We have gone from pricing a "blue wave" fiscal tsunami, to a "gridlock equals goldilocks" split Congress. Who knows, maybe we go back if we get a last-minute surprise out of the remaining Senate seats. The run-off in Georgia isn't until January 5th.

The Dollar

While global equities have come zooming back as they reprice political risk and look through the current COVID resurgence, the dollar is now at critical levels.

The interplay between FX and interest rates is always a big driver of financial conditions. The dollars role as global reserve currency makes the current levels in the dollar critically important. We are at an inflection point. Lower from here will help the global reflation story, higher will hurt it.

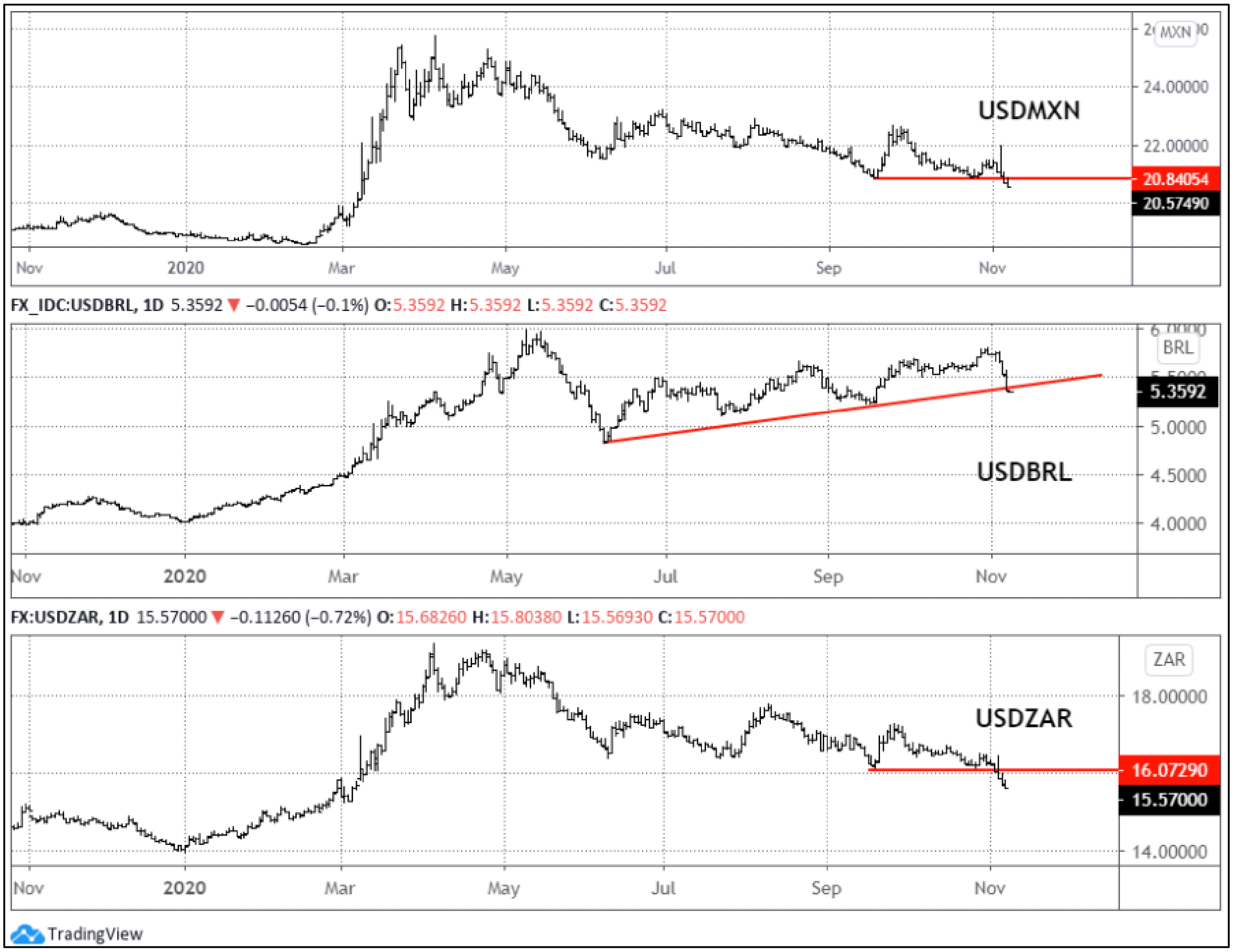
Vs. developed markets the dollar is sitting on support and threatening to break lower. A break now could deliver a quick 7-8% move vs. currencies like EUR, CHF, GBP, AUD, CAD, SEK.

In developed markets, currency strength is usually a cause for concern during disinflationary/ deflationary times. The ECB has already expressed concern about the strengthening EUR, expect others to follow if a USD drop really gets going. However, if EM also joins the party and the DM currencies don't look like they are exploding higher on a trade weighted basis as a result, they will have more patience with a higher currency resulting from global dollar weakness. There is some scope for that kind of EM outperformance here if we get some reflation traction.

Greater China FX has been doing well for a while now, on regional economic outperformance and better virus control.

Now we are starting to see some of the less favorable fundamental stories gaining a footing.

Countries like Mexico, Brazil and South Africa have been hit hard by both COVID and the global deflationary backdrop. For now, Turkey remains a fly in the EM FX ointment, with sentiment going from bad to worse.



Precious Metals

A meaningfully weaker USD would trigger a virtuous cycle for commodities as a whole and could be particularly impactful in triggering another leg higher in precious metals.

Here the interplay between longer-term yields and their effects on real rates have been a driver. However, so is the USD. A big move in the dollar can overwhelm gyrations in yield, especially if that narrative is adopted by the market.

Gold cracked its recent range. Let’s see if it can accelerate to the upside in the coming days.

Same story for Silver...

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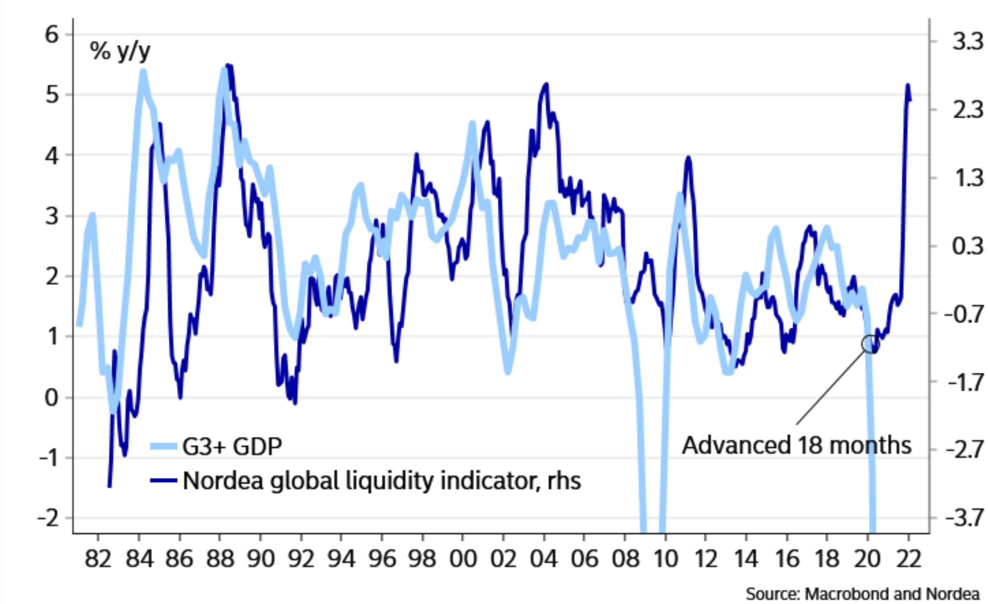
Bonds

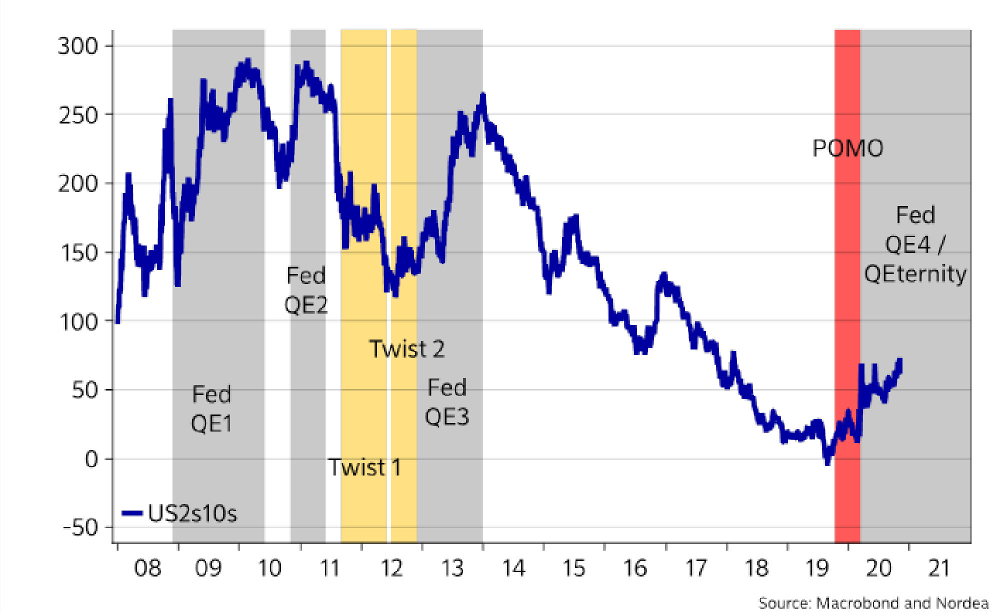
Bond yields quickly backed off last week as the lack of a "blue wave" became apparent. However, longer-term the huge amount of global stimulus is likely to kick in once a vaccine arrives and virus fears start to subside.

Chart 6. Strong global growth to be expected in 2021



As discussed in the past, QE should help steepen the curve if it stokes reflation hopes as it has in the past. Is QE's full effect on yields being held back like an underwater beachball by COVID? Or, is it a misfire this time? Let's hope it's the former.

Chart 2. The curve often steepens during QE programmes



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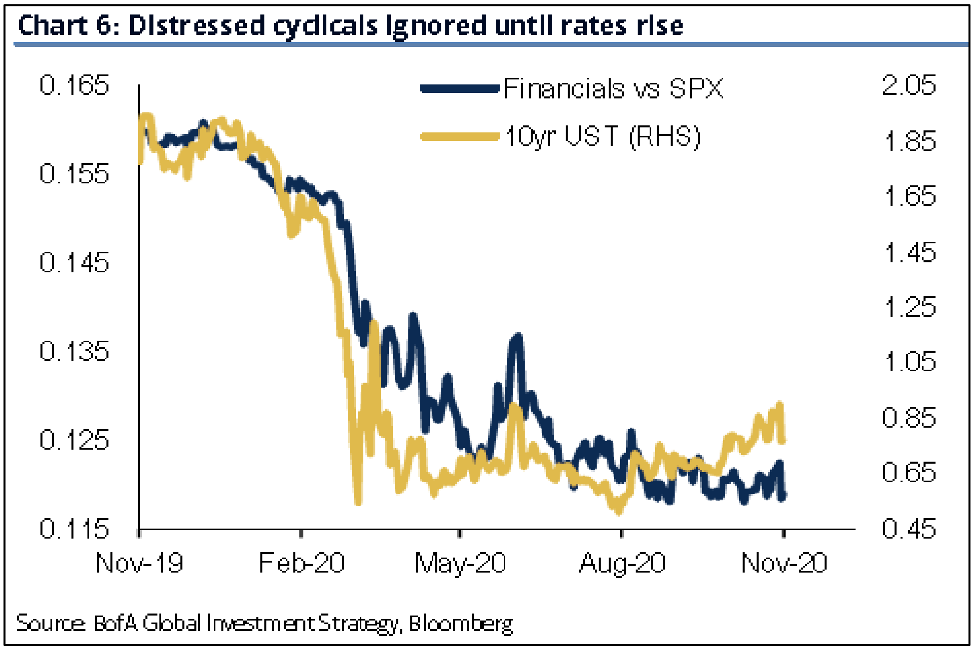
Equities

With the recent yield rise cut short, a breakout in financials was put back in cold storage for the moment.



More broadly, US equities are now back at the top of the recent range. Another dip before we push on? Or, does the momentum carry us higher?

Europe – We have come all the way back from an ugly break lower. Still no momentum on the upside as they continue to struggle with COVID, continued Brexit uncertainty, and now recent terrorism. Top of the range in France CAC40.

Spain is now trying to get escape velocity as well…

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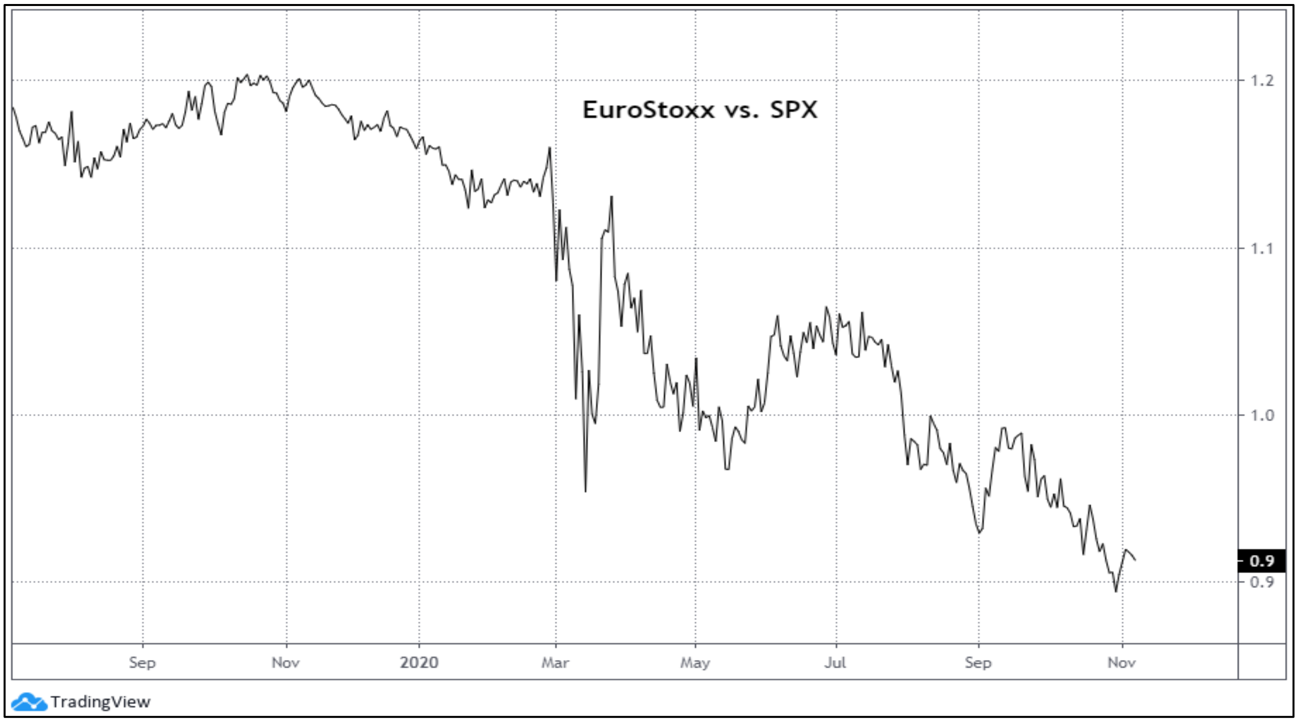
Having said that, still no sign that Europe is coming to life on a relative performance basis.



Japan – It has been a tough 3 decades for Japanese equities, but they are now testing what has been the top of a nearly 3-year range. It could run if we can clear these levels.

Even on a long-term relative basis, things may be looking up for Japan.

EM - As discussed, these markets are perking up as expected given the USD weakness. Brazil...

And Mexico...

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Important Macro Data Releases and Events for the Week

Monday
11/9/2020

- Trade Balance s.a. (Sep) Forecast: 18.2B, Prior: 15.7B
- BoE's Governor Bailey SPEECH
- Consumer Price Index YoY (Oct) Forecast: 0.8%, Prior: 1.7%

Tuesday
11/10/2020

- ZEW Survey - Economic Sentiment (Nov) Forecast: 63.7, Prior: 52.3
- ZEW Survey - Current Situation (Nov) Forecast: -65, Prior: -59.5
- ZEW Survey - Economic Sentiment (Nov) Forecast: 40, Prior: 56.1
- USDA WASDE Report
- Fed's Quarles SPEECH
- Fed's Brainard SPEECH

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Wednesday 11/11/2020	Veterans Day
	FDI - Foreign Direct Investment YTD YoY (Oct) Forecast:2.5%, Prior: 5.2%
Thursday 11/12/2020	BoE's Governor Bailey SPEECH
	Harmonized Index of Consumer Prices YoY (Oct) Forecast: -0.5%, Prior: -0.5%
	Economic Bulletin
	Industrial Production s.a. MoM (Sep) Forecast: 0.7%, Prior: 0.7%
	Initial Jobless Claims Forecast: - , Prior: 751m
	Initial Jobless Claims 4-week ave. Forecast: - , Prior: 787m
	Continuing Claims Forecast: - , Prior: 7.285m
	CPI ex-Food and Energy YoY (Oct) Forecast: 1.7%, Prior: 1.7%
	BoC's Wilkins SPEECH
	Fed's Williams SPEECH
Friday 11/13/2020	EcoFin Meeting
	GDP s.a. QoQ (Q3) Forecast: 12.7, Prior: 12.7
	GDP s.a. YoY (Q3) Forecast: -4.3, Prior: -4.3
	German Buba President Weidmann SPEECH
	Fed's Williams SPEECH
	PPI ex-Food and Energy YoY (Oct) Forecast: 0.9%, Prior: 1.2%
	Michigan Consumer Sentiment Index (Nov) Forecast: 82, Prior: 81.8

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