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What to focus on in Global Macro for the week of March 1st, 2021

Macro Themes on the Radar:

"…the best environment for stocks is a very dull, slow economy that the Federal Reserve is trying to get going." - Stan Druckenmiller

Last week we heard from a number of Fed officials, including Powell, Clarida, Brainard, Bullard and George. In the face of the accelerating run higher in bond yields last week, they all towed the same line. Basically, that the rise in yields reflects greater confidence in the economy and a reflationary backdrop. They continued to stick with the view that any near-term jump in inflation will be transitory and hammered home the commitment to lowering unemployment. Brainard, in particular, pointed out that they no longer see tight employment markets as predictive of inflation and are only focused on "shortfalls from maximum employment", rather than a more symmetrical approach. So far, no protest against the bond market selloff, although I would expect that the speed of the move is starting to raise some eyebrows internally, especially since it is starting to destabilize other markets. Interestingly, despite assurances from Powell that "the job is not done" and that it might take three more years to get their new broader view of employment where they want it, the markets have started to bring forward tightening expectations. It is rocking the boat for markets and I think we will see some pushback this week.

The jump in bond yields was not just a US thing but was global. Up until recently the ECB was more worried about the strength of the EUR, now it is yields. Various ECB officials have tried verbal intervention, saying that they are monitoring yields closely and that their bond buying flexibility will allow them to prevent tightening of financial conditions. Basically, threatening some form of YCC.

Australia is already engaged in YCC with a target yield for three-year paper. They had to intervene repeatedly last week.

Even Japanese yields have been pushed higher, although less dramatically.

All the CB's have the same concern, that a rapid and "premature" rise in bond yields will tighten financial conditions and be counterproductive to their efforts to reflate. It may end up mattering more to financial markets and maybe housing, than the rest of the economy given the vaccine rollout induced re-openings and the continued very large fiscal spending that is coming our way. This is the flipside of the idea that zero rates have a limited effect during a pandemic when the economy is artificially shut down.

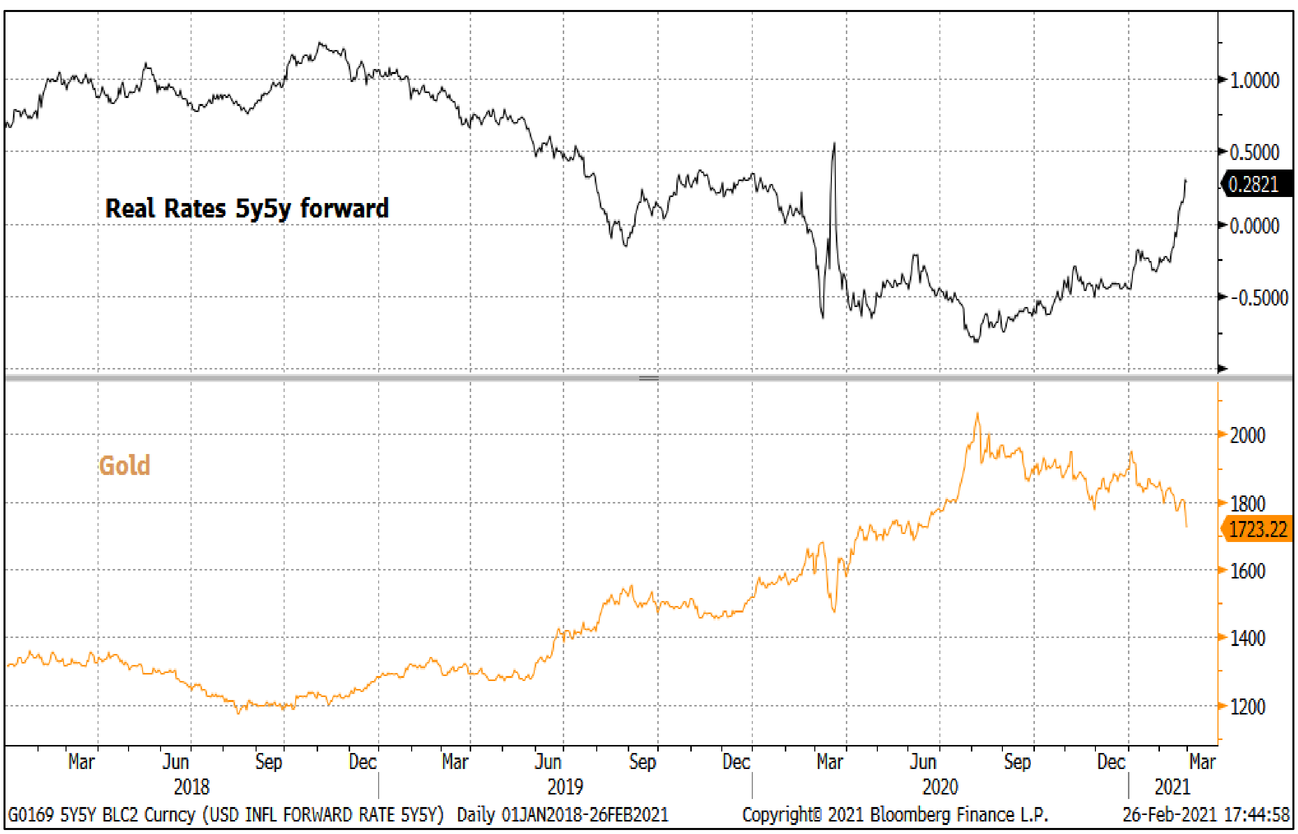
So why do CB's care if yields rise? It probably isn't the absolute level of yields… yet. However, it is happening too early for their taste, and now too quickly resulting in increased market volatility. A third reason could be that it potentially raises questions about further fiscal expansion. Can the government just keep spending without any consequences? Remember we had a couple of

Treasury auctions that went very poorly last week. With $1.9 trl in the works and hopes for potentially another $3 trl in some sort of infrastructure bill later in the year, is Treasury supply starting to become a factor? What the CB's do if they continue to be challenged will be very important. Will they dare to increase interference just as the growth and inflation prints are expected to jump? If so how? More QE or actually picking a spot on the curve as the RBA has done? As I said last week, this risks trying to put out the fire with gasoline. If they reduce the number of ways the market can express itself, it will increase the volatility in those that remain. After many years of suppressing volatility in financial markets, will the CB's now become its source?

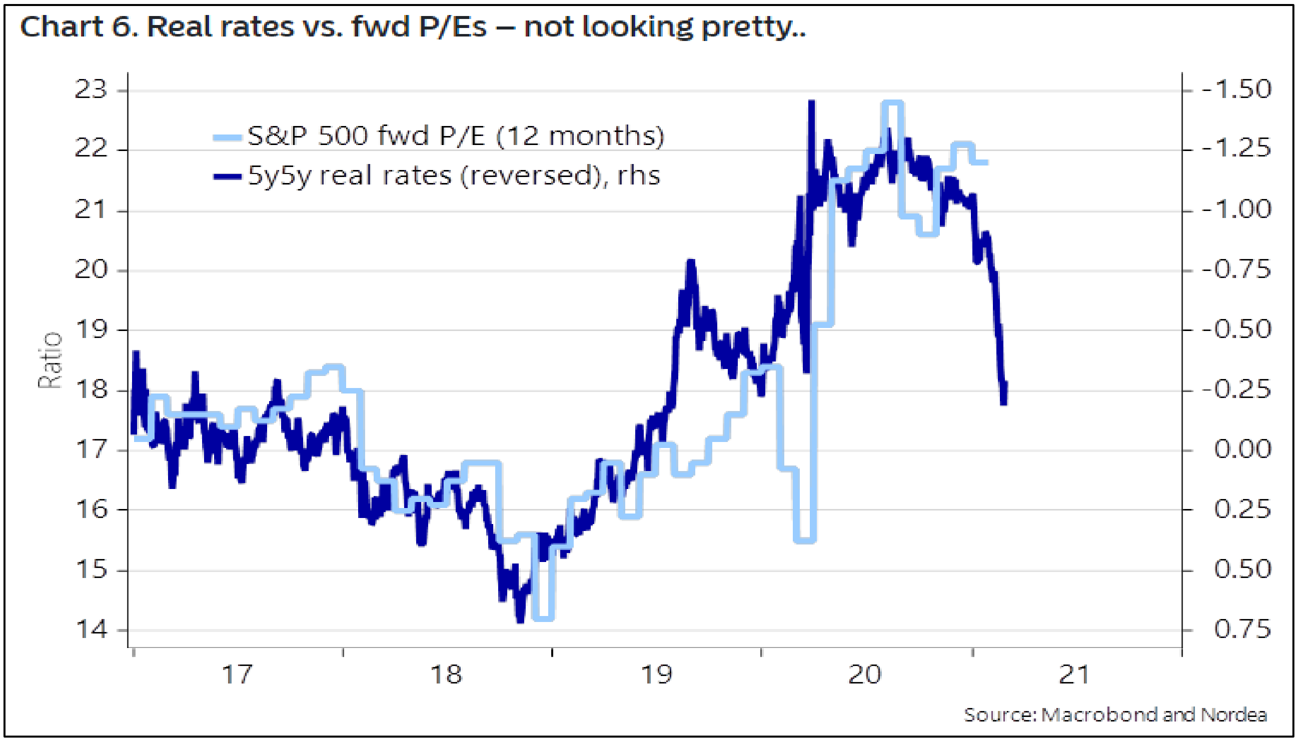
In the end, the Fed's reflation plans rest on their ability to generate commodity inflation that is then transmitted into goods and service inflation and wages. As commodity prices rise, inflation worries increase and people buy more commodities to hedge. So far self-perpetuating. However, if financial conditions suddenly tighten the feedback loop can break. A quick jump in bond yields can dampen inflation expectations as would a pop in the USD.

Real yields have been jumping as inflation expectations are slowly backing off while nominal rates pop. This move has implications across markets.

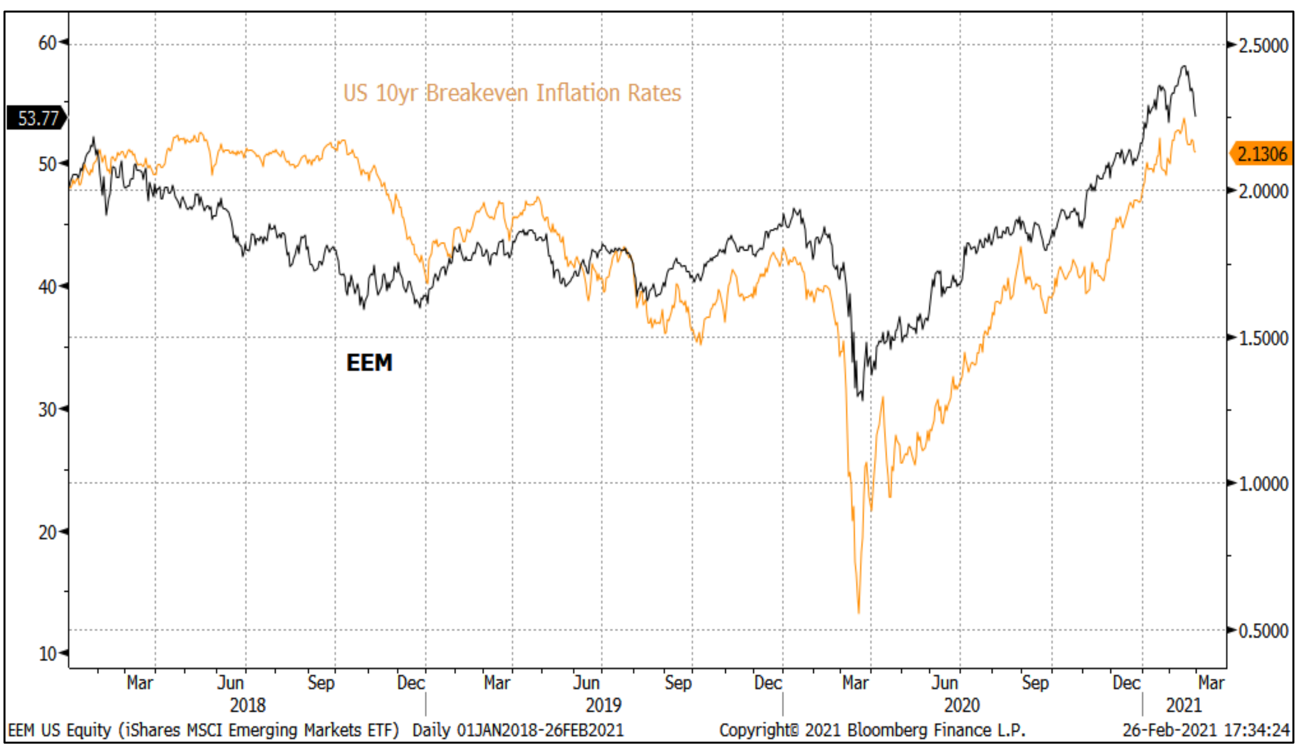
It has not been good for gold for instance…



The relationship to equity valuations is also giving people pause.



If we start to eat into inflation expectations, it will be hard on EM … where positioning is very extended.



What to Focus on Now:

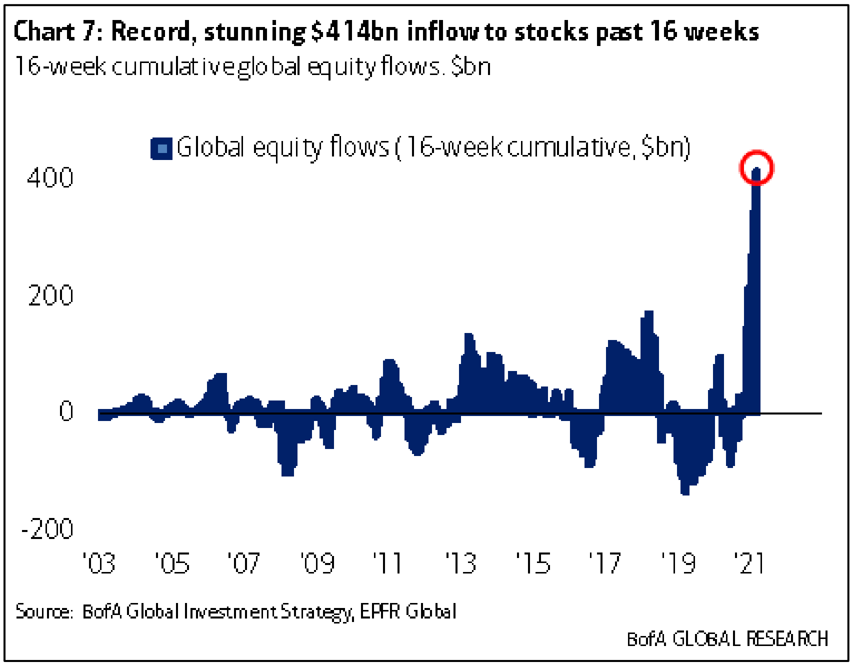
Last week the belly of the curve caught up. 5-year yields saw a huge jump as the market brought forward tightening expectations. 10-year yields had a big week as well but then retraced more than half the move on Friday.

However, as discussed this has been a global bond yield move over the last few weeks.

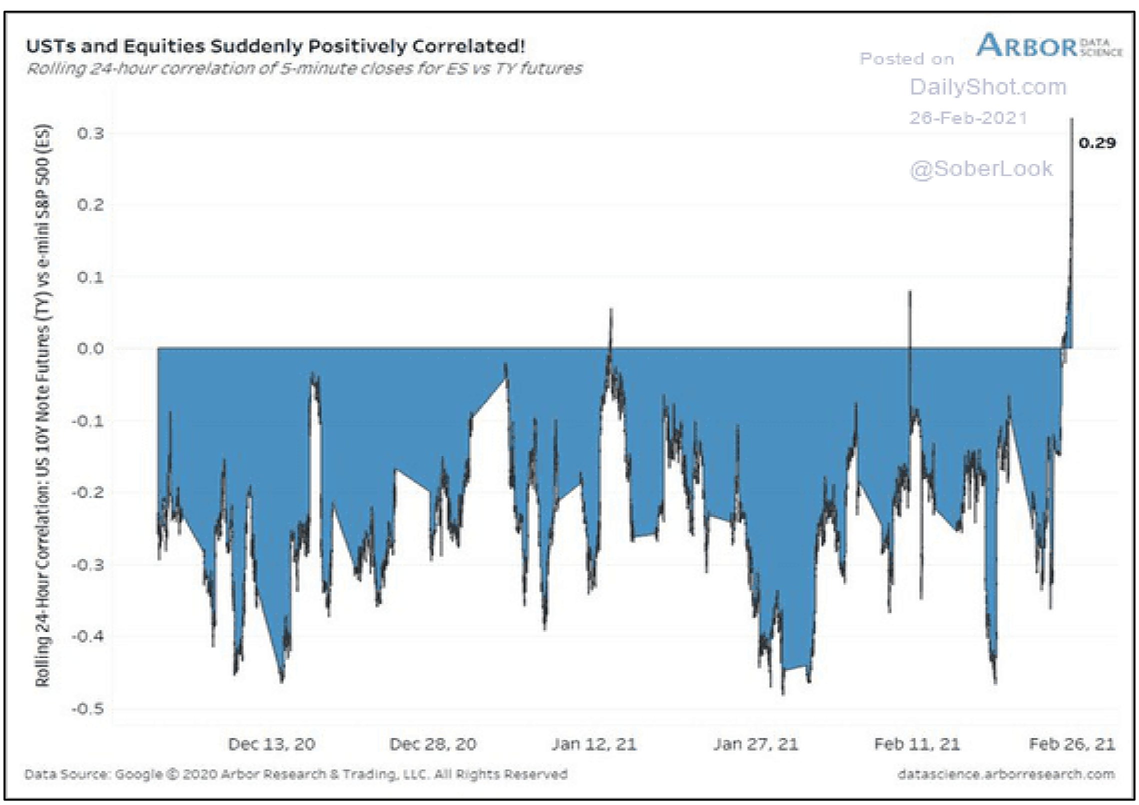
German Bunds…

and Japanese JGB yields have been on the move.

This potential new source of market volatility is hitting just as equity inflows have seen a very strong period.



Increased volatility and worries about early liquidity withdrawal took down both equities and bonds.



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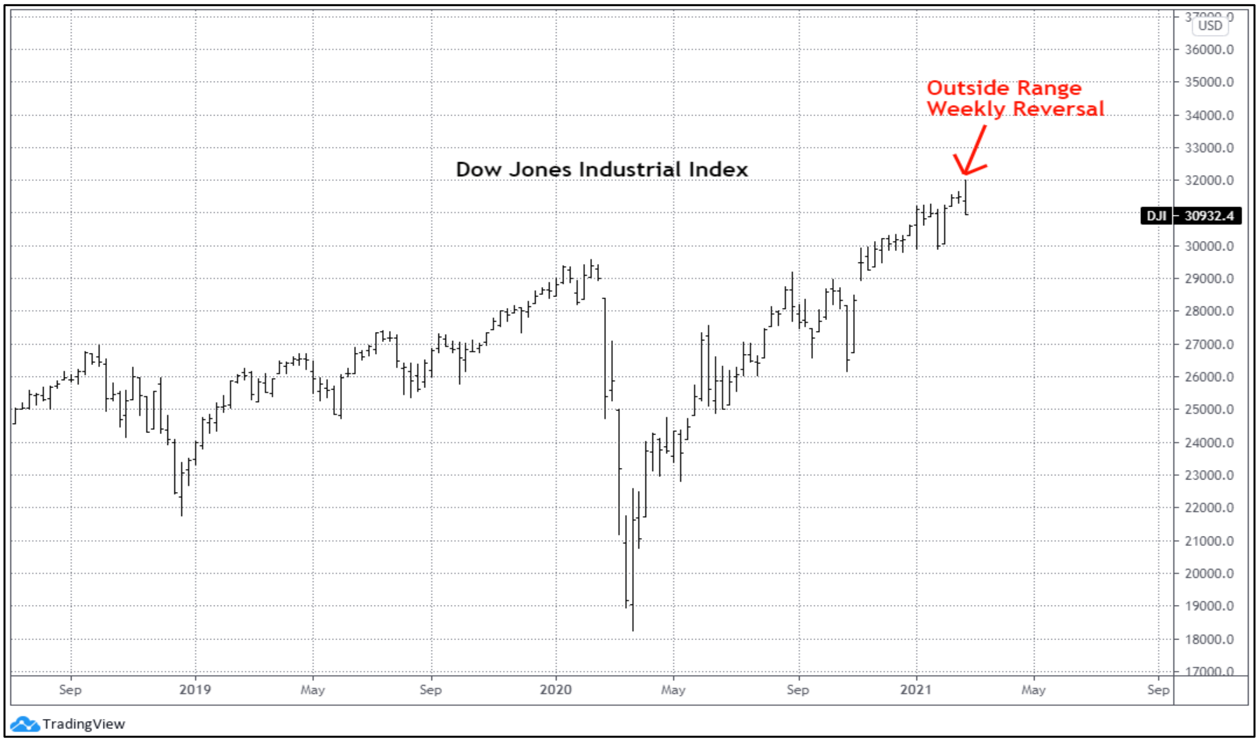
Early victims have been the most popular momentum plays. Plug Power is the largest holding.

ARKK's largest holding is Tesla

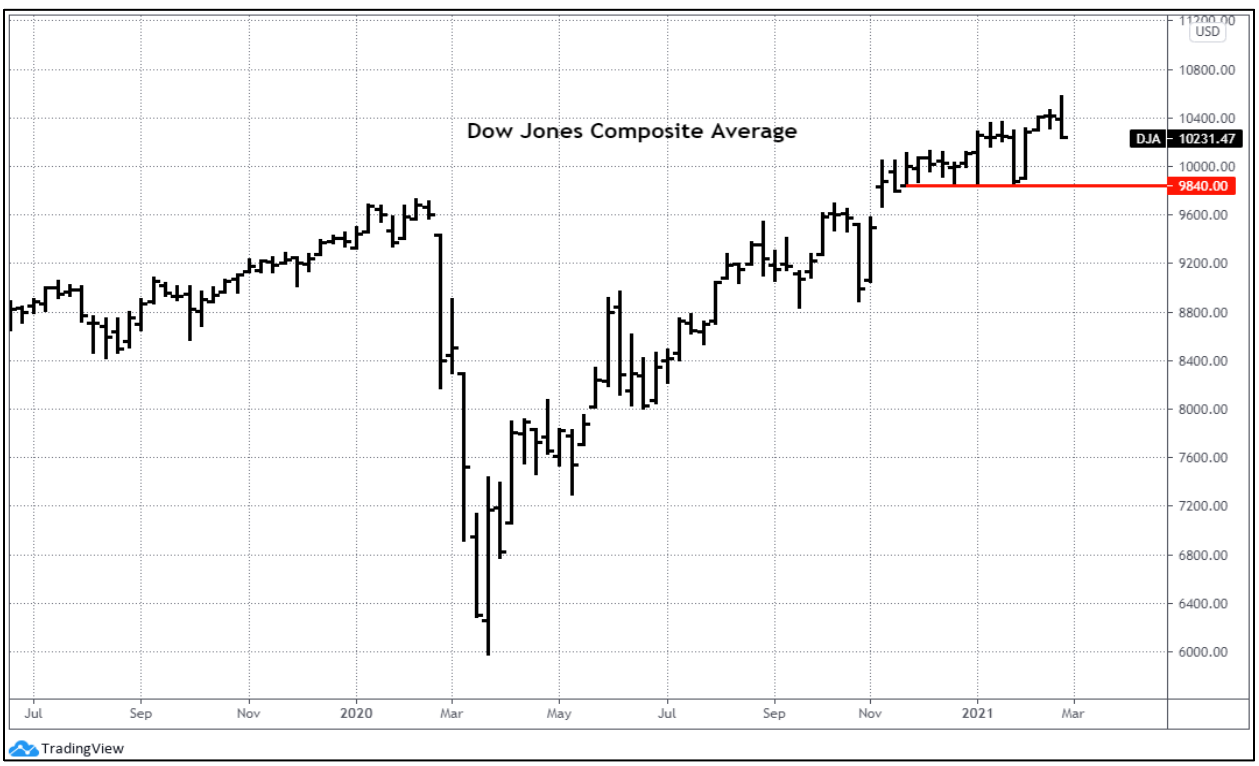
I would say that last week's price action leaves them on the defensive. They need to prove themselves in the near-term. We saw a big reversal week in the DJI after a strong start.



Higher yields have been pressuring the NDX in particular…momentum needs a quick recovery.

The weekly chart did some damage as well.

The DJ Comp needs to hold the 9840 level in the coming weeks.



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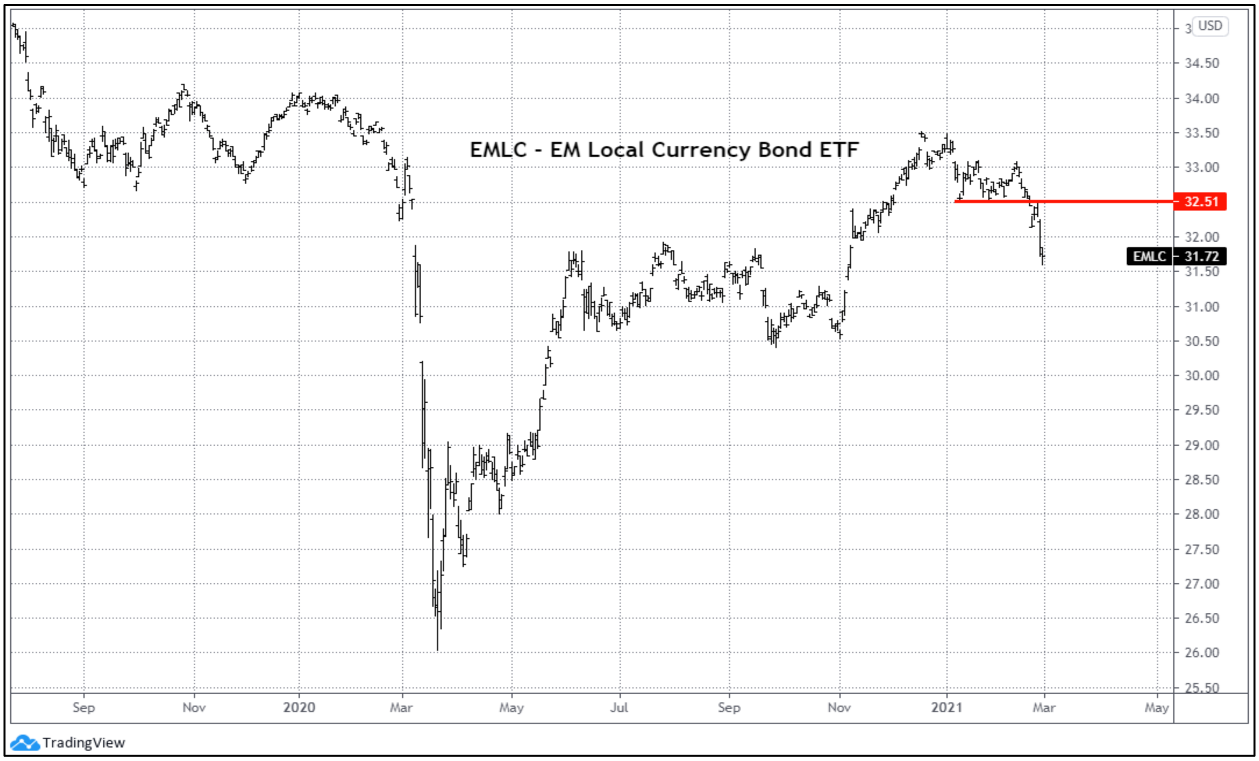
Given the yield move, it is no surprise that part of the Comp's problem is the Utilities sector.

As discussed, the jump in yields is also weighing on Emerging Markets. Holding so far.

With already tight spreads EM bonds are feeling the heat from higher global yields.



That could accelerate for the local currency versions if the dollar advances here.

In FX world the end of the week brought lots of reversals. AUD saw an impressive outside range weekly reversal.

As did USDNOK…

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and USDSEK

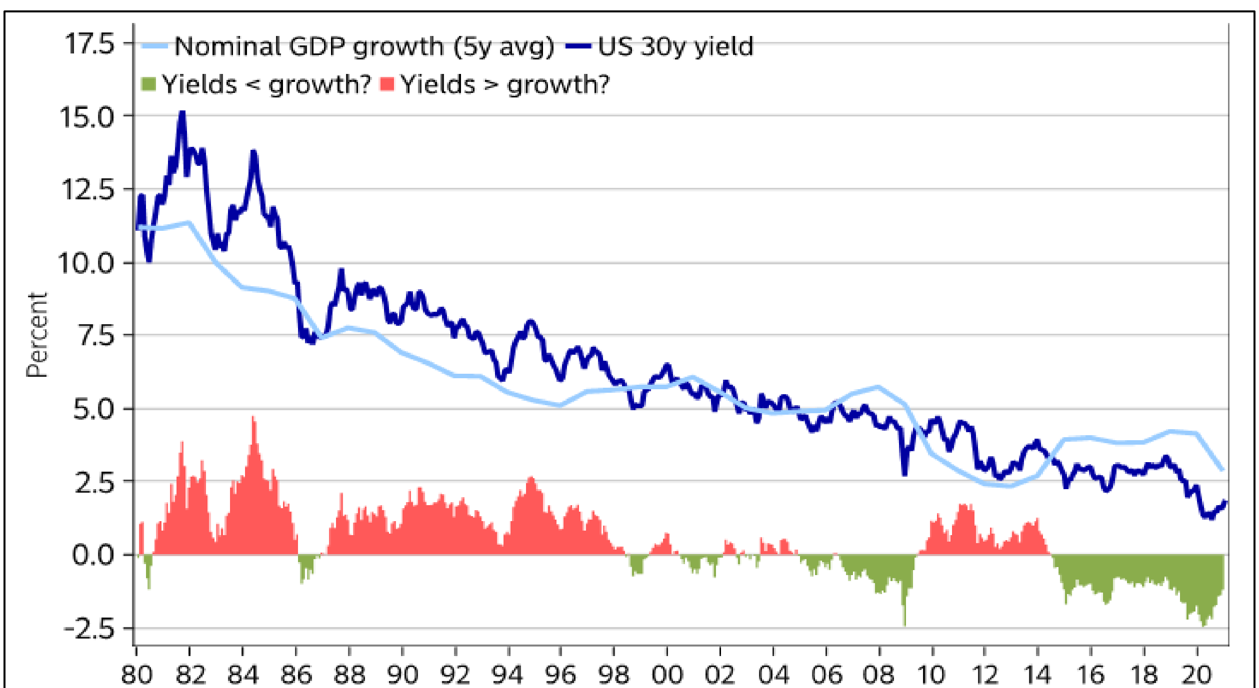
USDCAD was right on the edge and right up against the downtrend. Smells like higher USD.

The EUR also had a very steep reversal from new 6-week highs only two days earlier.

USDJPY and USDCHF which are sensitive to the yield move made new highs for the run.

I like long volatility in these. Volatility is cheap and lots can happen here in the next few weeks.

Last note … I thought this was an interesting chart given last weeks discussion about periods when the market fears inflation vs. fears deflation. We are making a big jump with the new Fed framework and entering a period of opportunistic reflation vs. the period of opportunistic disinflation that the Fed engaged in from the early '80's until '98.



Source: Macrobond and Nordea

It is a week full of potential tape bombs. We have global PMI during the week and the US employment report on Friday. We also have lots of Fed and ECB speakers starting Monday with ECB President Lagarde and wrapping up with a potentially impactful speech from Fed Chair Powell on Thursday.

Important Macro Data Releases and Events for the Week

Monday
3/1/2021

- (Sunday night) Caixin Manufacturing PMI (Feb) Forecast: 51.5, Prior: 51.5
- Manufacturing PMI's across Europe
- Harmonized Index of Consumer Prices YoY (Feb) Forecast: 1.6%, Prior: 1.6%
- Fed's Williams and Brainard both have speeches
- ISM Manufacturing PMI (Feb) Forecast: 58.9, Prior: 58.7
- ISM Manufacturing Prices Paid (Feb) Forecast: 77, Prior: 82.1
- ECB's De Guinos and President Lagarde both have speeches
- RBA Interest Rate Decision and Statement - Current 0.1%

Tuesday
3/2/2021

- CPI YoY (Feb) Forecast: 1%, Prior: 0.9%
- ECB's Panetta speech
- Fed's Brainard speech
- Caixin Service PMI (Feb) Forecast: -, Prior: 52

Wednesday
3/3/2021

- Service PMI's across Europe
- Buba President Weidmann speech
- ECB's Panetta speech
- ADP Employment Change MoM (Feb) Forecast: 168k, Prior: 174k

	Markit Service PMI (Feb) Forecast: 58.9, Prior: 58.9
	Markit Composite PMI (Feb) Forecast: 58.8, Prior: 58.8
	ISM Services PMI (Feb) Forcast: 58.7, Prior: 58.7
	ISM Services Prices Paid (Feb) Forcast: 64.7, Prior: 64.2
	ECB's De Guinos and Schnabel both have speeches
	Fed's Beige Book
Thursday 3/4/2021	Retail Sales YoY (Jan) Forecast: -1.3%, Prior: 0.6%
	Unemployment Rate (Jan) Forecast: 8.3%, Prior: 8.3%
	Initial Jobless Claims Forecast: 755k, Prior: 739k
	Initial Jobless Claims 4-week average Forecast: -, Prior: 807.75k
	Continuing Jobless Claims Forecast: -, Prior: 4.419m
	Nonfarm Productivity (Q4) Forecast: -4.7%, Prior: -4.8%
	Factory Orders MoM (Jan) Forecast: 1.9%, Prior: 1.1%
	Fed's Chair Powell SPEECH
Friday 3/5/2021	**Nonfarm Payrolls (Feb) Forecast: 148k, Prior: 49k**
	Unemployment Rate (Feb) Forecast: 6.4%, Prior: 6.3%

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