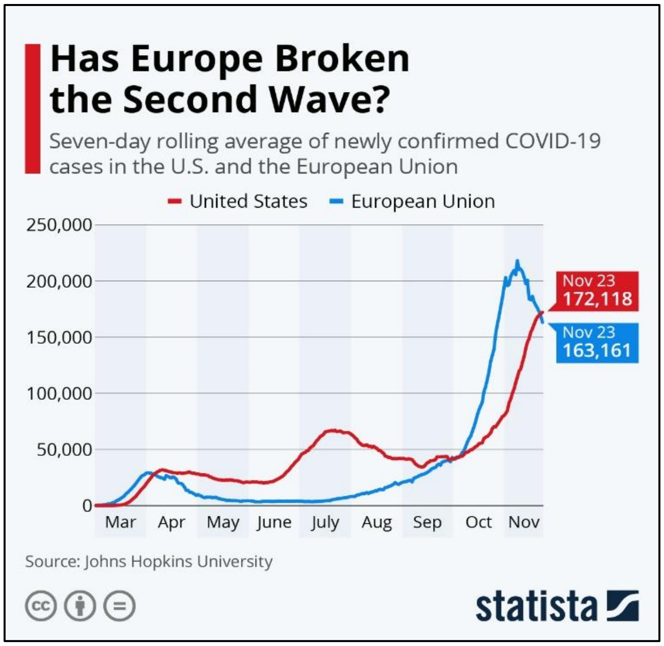
Stargazer
Asset Management

What to focus on in Global Macro for the week of November 30th, 2020

Macro Themes on the Radar:

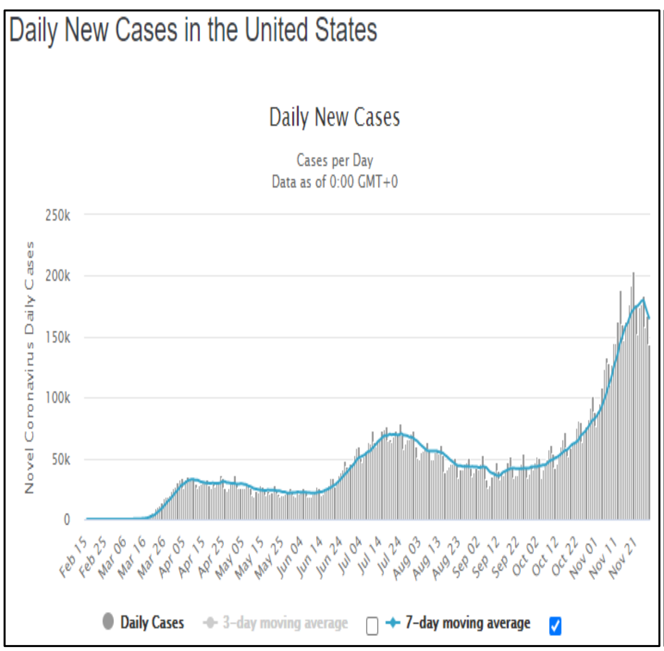


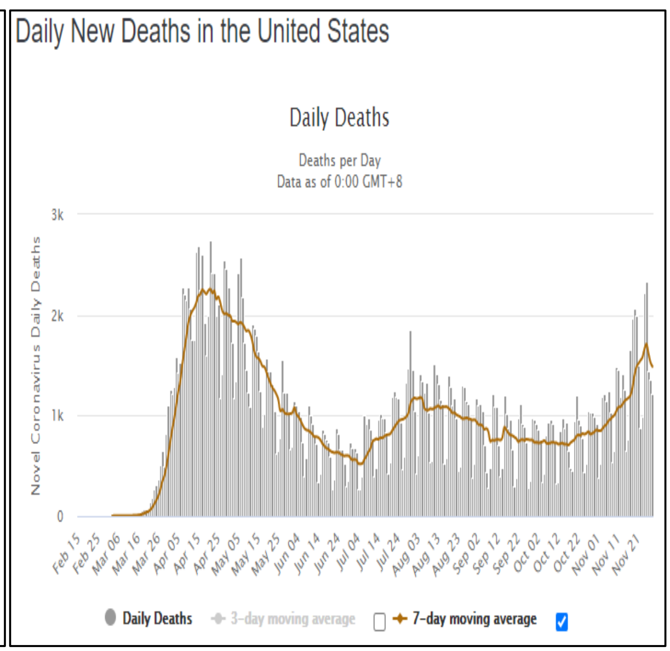
While there is a lot of variation between countries, in aggregate EU new cases data looks to have turned a corner.

The latest US data is showing signs of peaking as well, although the effects of the Thanksgiving holiday won't be known for a week or more.

Bond yields and equities will be watching carefully for hints that the near-term virus outlook is improving enough to hold off concerns about a postponed recovery.

In the US, weekly unemployment claims have been ticking higher and in Europe data has been weakening.





So far markets have been looking past the near-term challenges, possibly with the exception of bonds that have continued to hold up better than might be expected given what is being priced in other markets.

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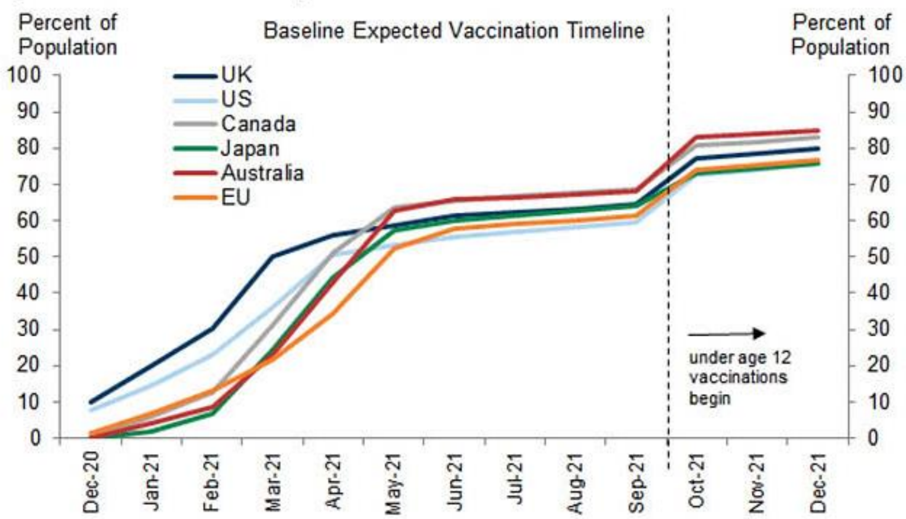
Increasingly, analysts see most DM economies reaching herd immunity via vaccination and recovery by mid-year.

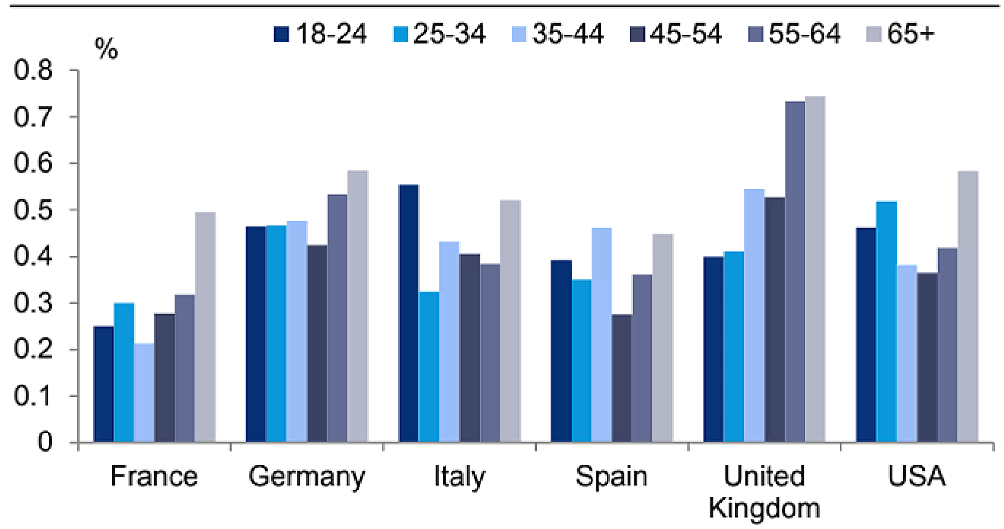
Exhibit 4: Under Our Baseline Forecast, Large Shares of the Population Are Vaccinated by the End of Q2 in All Major DMs



Source: Goldman Sachs Global Investment Research

Although, willingness to be vaccinated early on, varies considerable by country and age group.

Proportion of residents planning to be vaccinated against Covid-19 within 3 months of vaccine availability (November data)

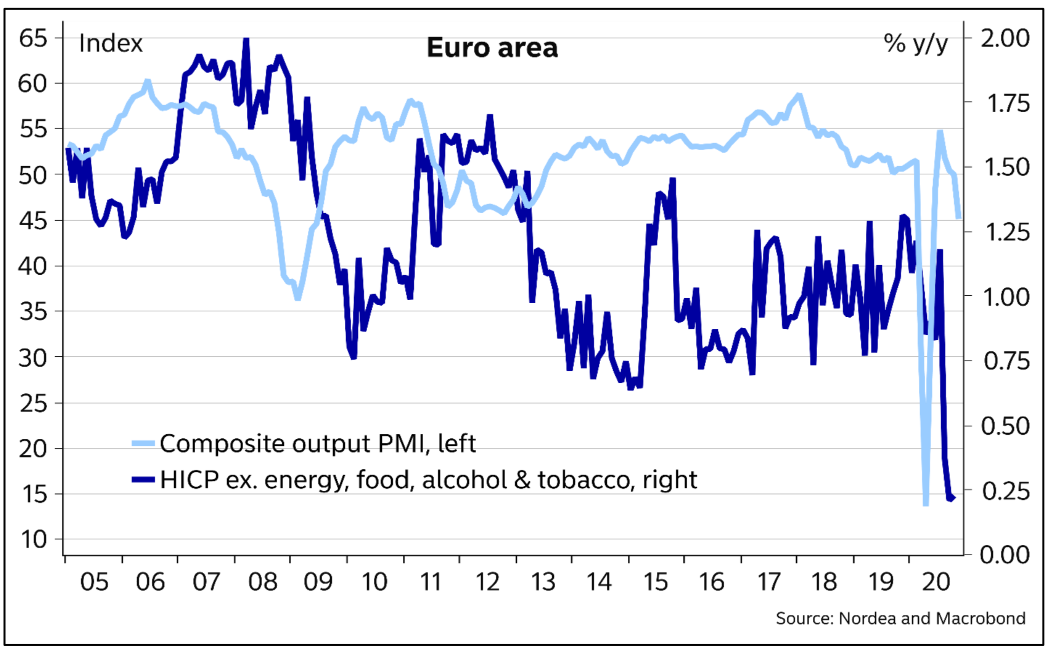


source: dbDIG Primary Research

However, as it becomes more widely available and hopefully with a low incidents of side effects, its popularity should jump. Expect there to be exclusions from certain activities for un-vaccinated individuals, and that should force the uptake. For example, US Colleges and Universities are talking about proof of prior infection or vaccination being required for attendance. Airlines are increasingly talking about requiring proof of vaccination as are movie theaters. By March/April, the number of vaccinated should already be making a meaningful difference to infection rates. This is what markets are increasingly pricing, but with a lot of uncertainty around the near-term outlook and the potential for long lasting effects to the economy, even after the pandemic has passed.

ECB

As the December 10th ECB policy meeting approaches, it is expected that new easing will be focused on PEPP and TLTRO's. The latest round of lockdowns has again slowed economic activity and they have essentially pre-announced further action. Increasing the rate of asset purchases may be difficult without expanding the scope. If there is a surprise, it will probably be in what they are willing to buy. At a minimum, expect an increase of total purchases under PEPP by EUR 500bln and an extension of the program duration. Expect further strong calls for fiscal spending with monetary policy at or near its limits.



Watch for comments regarding EUR strength. In the past the ECB has worried that a stronger EUR could "hinder monetary policy transmission." However, if European equities continue to rally or at least maintain the recent gains, this could be less of a concern as it would counteract any tightening of financial conditions from a stronger currency. A further EUR rally as part of a general USD decline would also be less worrying. In either case, outside of some unlikely measures there really isn't much the ECB can do about the EUR at the moment.

Treasury Secretary

As the likely Biden cabinet takes shape it is worth noting that it seems to almost entirely exclude the progressive wing of the party. Nominations are focused on individuals who have previously served under the Clinton and Obama administrations. Janet Yellen is no exception. While she is certainly an establishment pick, she comes with a lot of clout given her previous term as Fed Chair. She was seen as a dove at the Fed, with an inclination to "let it run hot" as the benefits of a tight labor market outweighed the risks of potentially higher inflation down the road. This is a mindset that has been increasingly adopted inside the Fed given the continued low inflation, COVID fallout and feedback from programs such as Fed Listens. She is open to new ideas and back in April of this year suggested that Congress should look at broadening the Fed's list of tools to include purchasing equities outright. We can expect very tight cooperation between the Fed and Treasury going forward. Together expect them to put a lot of pressure on Congress to act on fiscal issues, or to find go-arounds.

Reflation, Deflation or Debt Jubilee

With global rates at zero or negative, bond yields have also been glued to the floor. Increasingly we have CB's talking about CBDC's and the likes of the IMF pondering if we have arrived at a new Bretton Woods moment, requiring a reset of the global financial order. There is talk about debt cancellation and forgiveness. On the fringes there are people calling for CB's to cancel some of the bonds they have purchased during QE, maybe doing it in a coordinated manor across G7, popping everyone's money supply simultaneously. More mainstream, we recently saw suggestions from Italy (made by PM Conte's top advisor) that the ECB should cancel or perpetually hold Italian debt issued during the pandemic. The ECB quickly pushed back as you might expect, but now it is out there. This Bloomberg article on the subject is worth a read.

These topics remind me of the MMT discussion that has become increasingly mainstream. Unimaginable, until it isn't. While not MMT per se, the idea that governments can run much larger deficits than thought, without any apparent consequences has made markets giddy. COVID has broken the taboo. COVID and its aftermath may yet break other taboos.

While some of these ideas may seem outlandish and like too big a leap, policy makers are now much less constrained by institutional inertia than they were only a year ago… if not this crisis then the next.

What to Focus on Now:

With the vaccine providing light at the end of the tunnel, markets continue to be in "risk-on" mode.

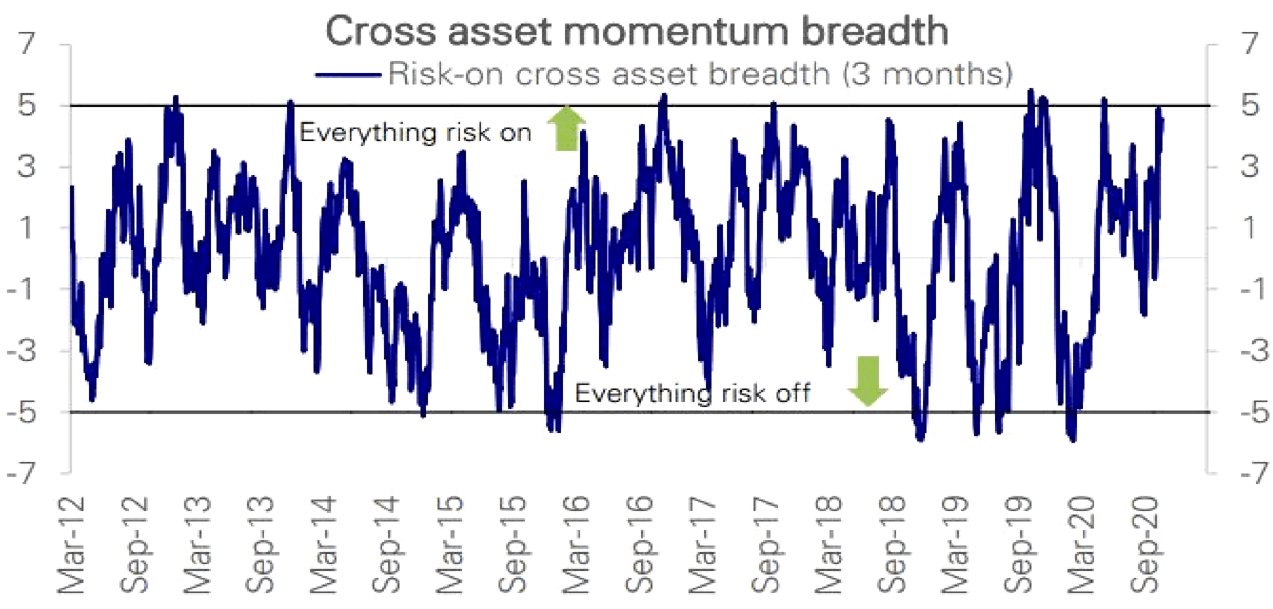


Figure 4: Cross asset momentum breadth is at the top of its historical range

Note: Sign reversed for Gold, US rates and German rates

Source : Bloomberg Finance LP, Deutsche Bank Asset Allocation

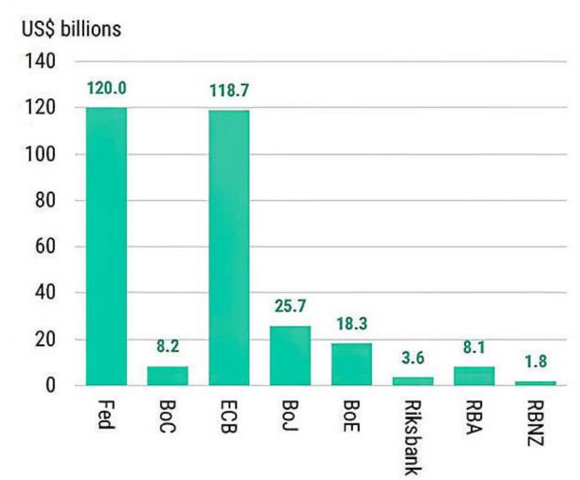
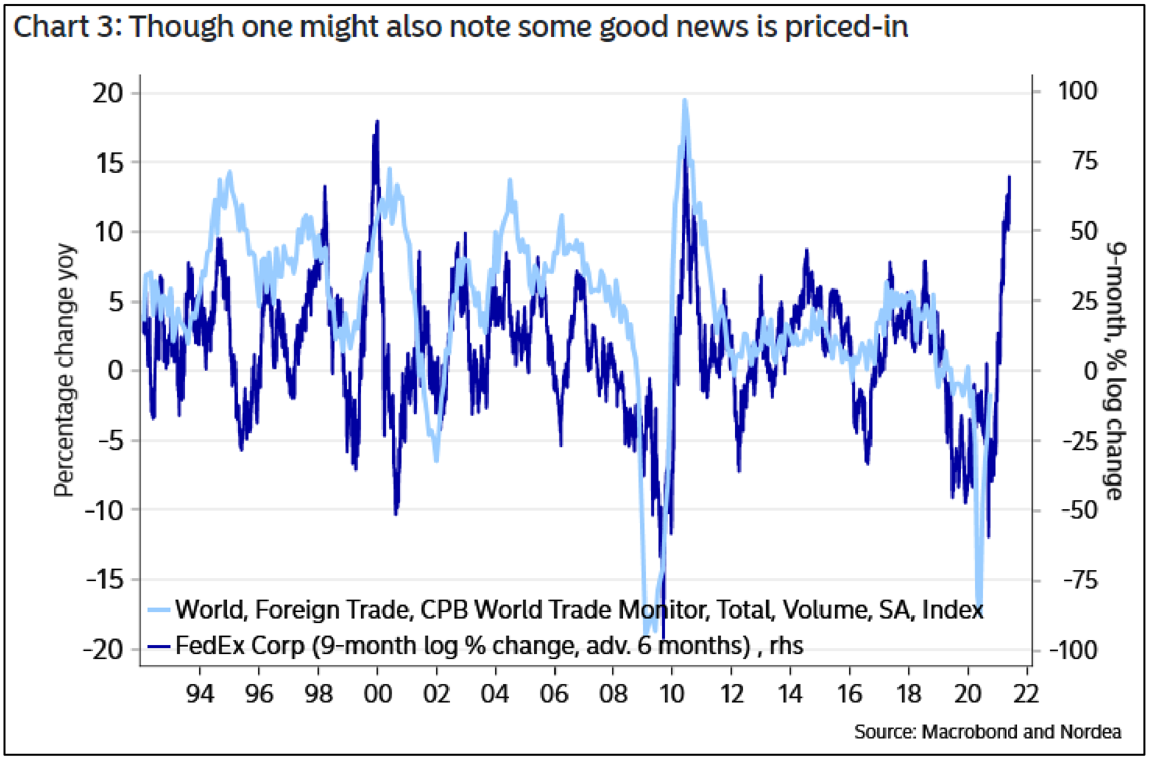


Exhibit 8: G10 central bank expected average monthly QE pace in 2021, in USD

Source: Morgan Stanley Research, National central banks, Bloomberg

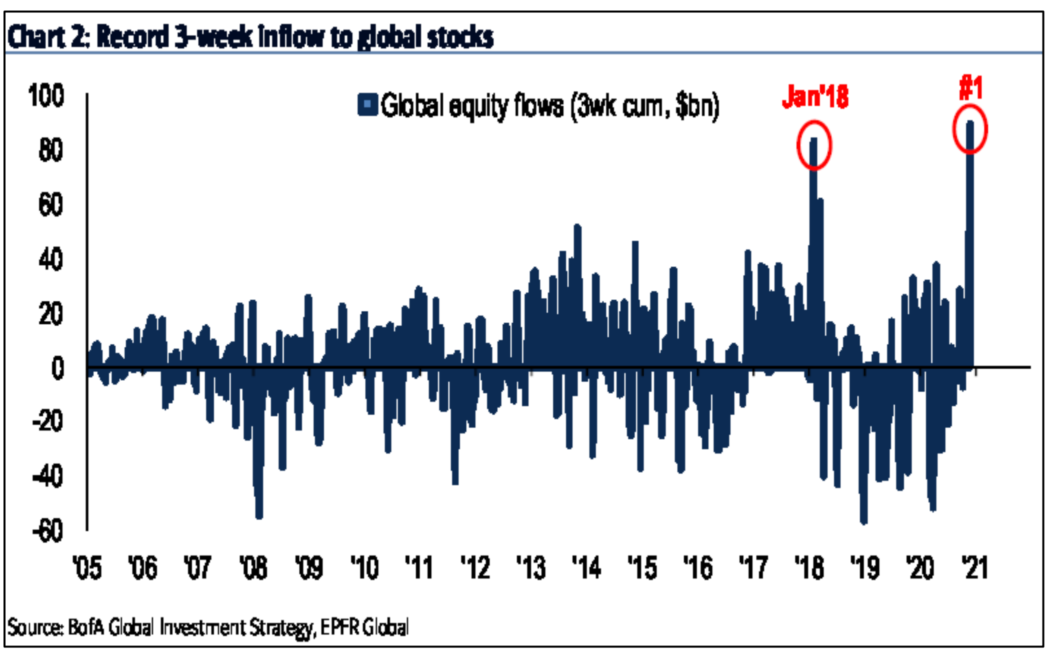
Markets continue to look through the near-term concerns and on to a 2021. It is expected that CB's and governments keep pumping monetary and fiscal stimulus, while global GDP's and trade recover, pushing up corporate earnings.

"Though one might note some good news is priced-in" as Nordea Research points out in the following chart…

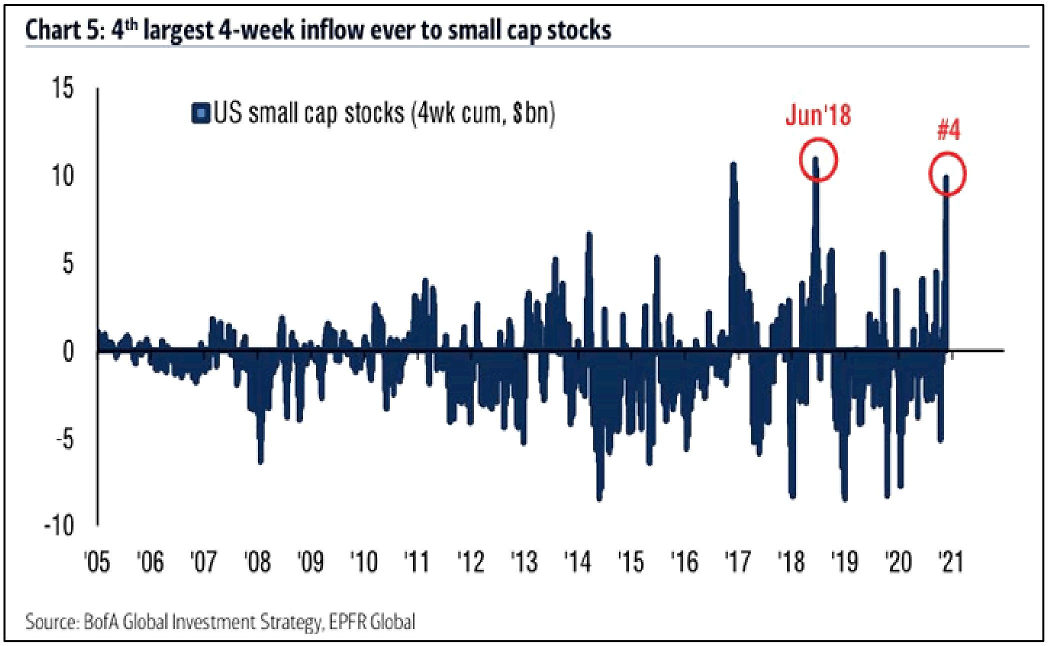


Equities

The flow into equities has been record-breaking. Sell low buy high over the last few years has not done investors any favors. These extremes have made for very unstable markets in recent years.

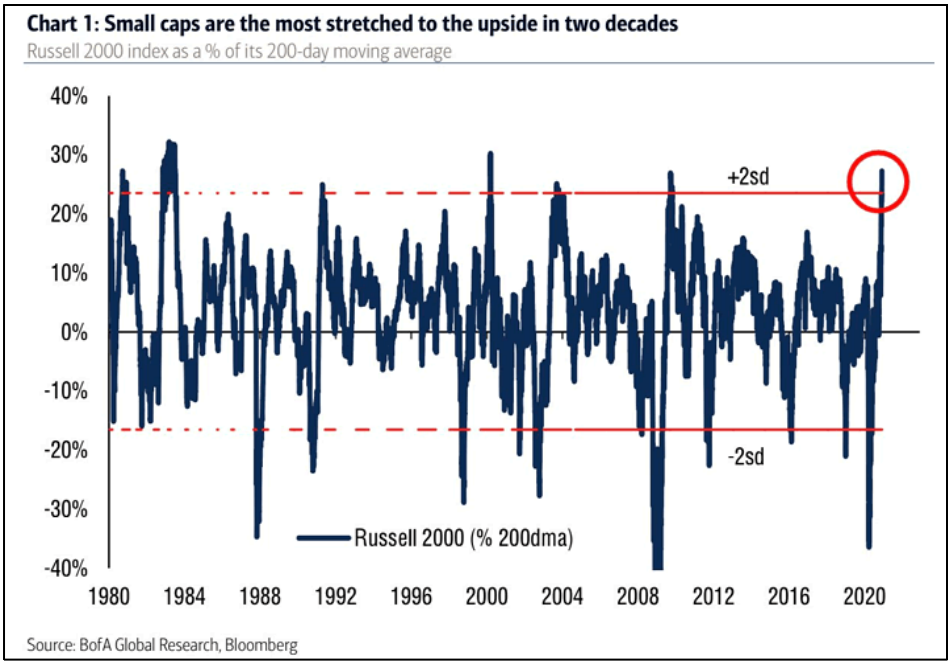


Flows into small caps have been driving some of the inflow.

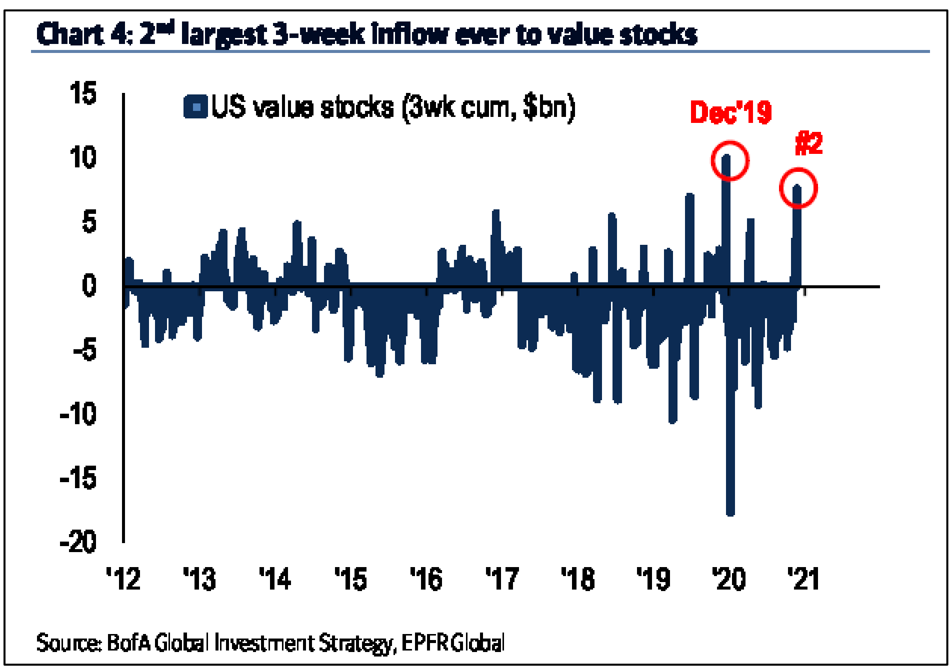


The Russell 2000 has had a nice break higher vs. the S&P as a result. Prior inflow extremes in early '17, mid-'18 didn't turn out so well on a relative basis. This time could be a bit different given where we are coming from, but bond yields may need to re-engage on the upside to provide support.

However, the run has been blistering. This pace likely can't continue.



Value stocks have obviously also been on a tear as the rotation has gone into full swing.



Again, flows have been big. This is a big field so some of the more dramatic moves in things like energy are watered down in the index making the relative move look far less impressive.

If this is the start of a real recovery in value, (we will need some really broad-based growth for that) then what we have had so far on a relative basis is meaningless. Don't forget this line of thinking can be a bit misleading because growth has had the beta, and during the last value/growth outperformance it was the fall in growth (NDX crash) that took the ratio up.

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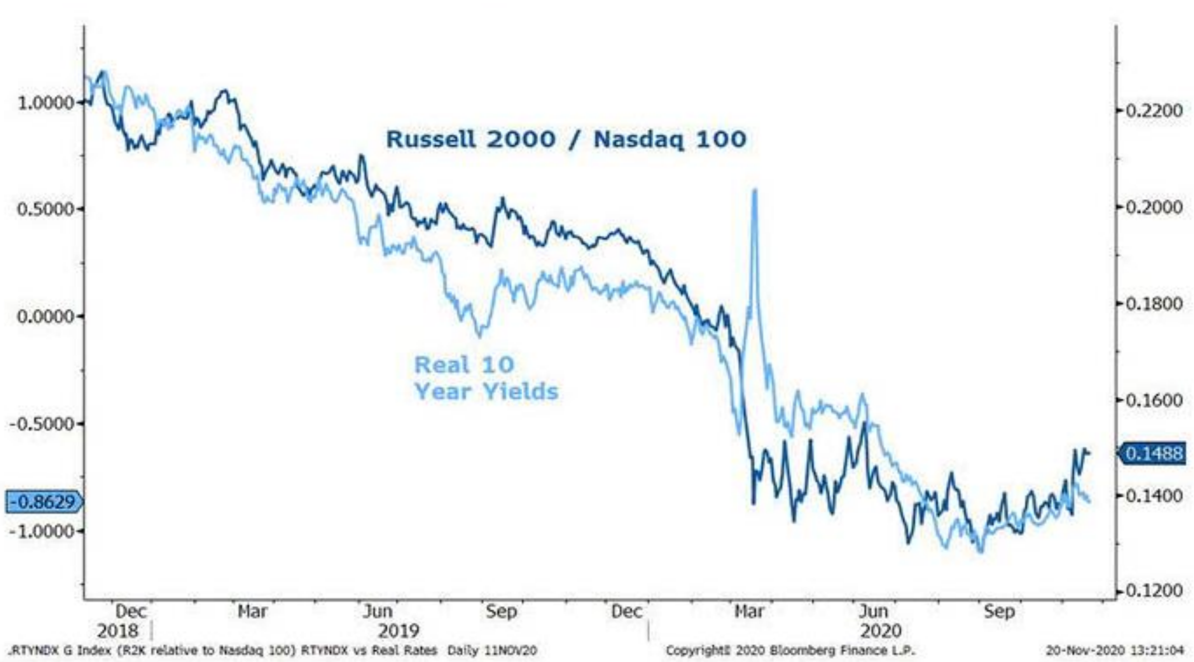
So far, cyclicals are looking good. Eventually long end yields should concede. If they don't or break lower again be careful of at least a temporary narrative shift.

Exhibit 6: Equity Market Internals Continue to Point to Higher Rates

source: Morgan Stanley

Exhibit 1: New leadership is emerging and rates play a big role



Source: Bloomberg, Morgan Stanley Research

Over the last few weeks, the Nikkei blasted through the top of its nearly two-year range. The vaccine news was clearly a big help. However, interest in Japan had been growing and those headlines were the green light. The amount of fiscal stimulus Japan has been engaged in has been gigantic, nearly double that of the US as a percentage of GDP. Usually they like to follow up with a recovery crushing tax hike. This time there hasn't been any talk of that. Another example of the MMT infused mood governments are in?

There is even hope that the long-term relative picture could be turning for Japan.

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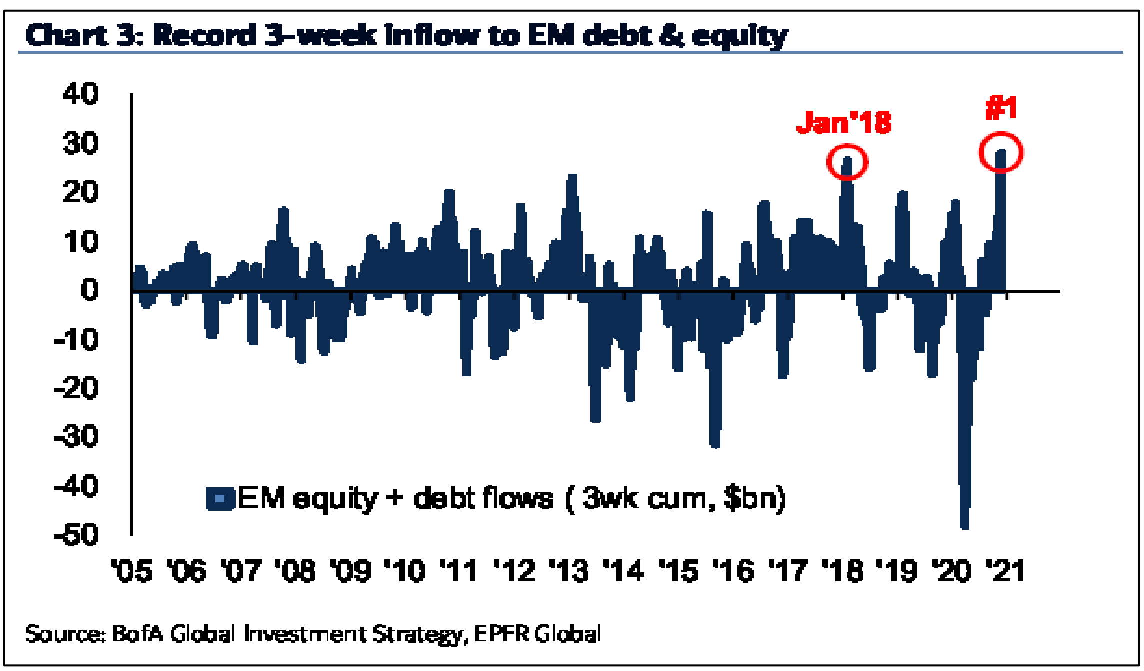
European equities have so far been able to maintain the explosive post vaccine move. I think you will most likely get better levels to buy, but so far there has been no retracement.

The bulk of a move in Spanish equities I envisioned over a few months, happened in a few days.

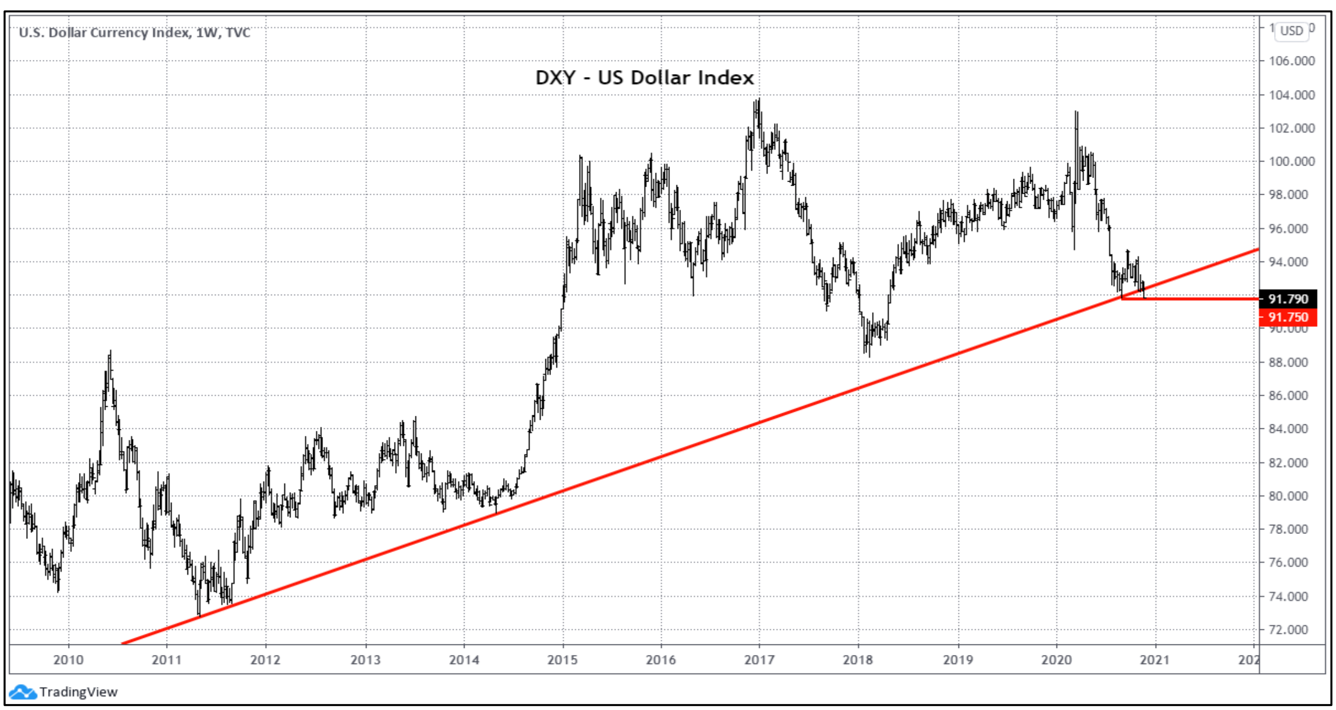
On a relative basis the move off the lows for Europe has been impressive as well. We are now at levels from which a further move could indicate that a longer period of outperformance could be in the cards.

EM has also seen large inflows, as the global growth for value switch spreads in anticipation of higher growth and a weaker USD.



The EM underperformance since 2011 has been relentless with the exception of a two year pause between 2016-2018. Now, that downtrend is in question. A break higher, if sustained, would herald a potentially very large global asset reallocation. The USD is key.

FX - The dollar is teetering on support here. The 1.20 level in the EUR is worth watching as is 91.75 in the DXY (last low). If bonds are stuck, the USD could be the initial reflation tell.



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It is decision time for FX. The EUR is now at one of our inflection points from which prices tend to either quickly reverse OR accelerate sharply.

If dollar falls there will be lots of ways to express it across DM and EM.

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Bonds – This is a tricky chart as we risk a failure of the breakout in 30-year yields. It could just be the near-term COVID lockdown drag but needs to be watched for all the obvious ties to everything from equity rotation to the USD and risk-on in general.

10's have not been able to crack the downtrend in yield… not great price action.

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Gold

After large selling over the last few weeks Gold broke the big 1850 level it had been holding. Maybe we don't need safe havens if growth is back… This is the flipside of expected higher yields knocking down Gold via real rates. For now, I think the 1700-1750 is a buy zone. If the USD does start to fall more meaningfully here it will support Gold, especially if yields can't rise. Worth keeping on your radar for a good entry given the continued CB and fiscal backdrop.

Important Macro Data Releases and Events for the Week

Monday
11/30/2020

- Non-Manufacturing PMI (Nov) Forecast: 52.1, Prior: 56.2 (Sunday night)
- NBS Manufacturing PMI (Nov) Forecast: 51.5, Prior:51.4 (Sunday night)
- OPEC Meeting
- Harmonized Index of Consumer Prices YoY (Nov) Forecast: -0.5%, Prior: -0.5%
- Chicago Purchasing Managers Index (Nov) Forecast: 59.2, Prior: 61.1
- Pending Home Sales MoM (Oct) Forecast: 1%, Prior: -2.2%

RBA Interest Rate Decision and Policy Statement

Tuesday
12/1/2020

EcoFin Meeting

Markit Manufacturing PMI's for various EU countries

CPI - Core YoY (Nov) Forcast: 0.2%, Prior: 0.2%

CPI YoY (Nov) Forcast: -0.2%, Prior: -0.3%

Fed's Chair Powell testifies / Senate

ISM Manufacturing PMI (Nov) Forecast: 57.5, Prior: 59.3

ISM Manufacturing New Orders Index (Nov) Forecast: 53.4, Prior: 67.9

Wednesday
12/2/2020

Retail Sales YoY (Oct) Forecast: 6.6%, Prior: 6.5%

Unemployment Rate (Oct) Forecast: 8.4%, Prior: 8.3%

ADP Employment Change (Nov) Forecast: 420k, Prior: 365k

Fed's Quarles SPEECH

Fed's Chair Powell testifies / House

Fed's Williams SPEECH

Fed's Beige Book

Trade Balance MoM (Oct) Forecast: 5800M, Prior: 4840M

Thursday
12/3/2020

Markit Services PMI's for various European countries

Initial Jobless Claims Forecast: 770k, Prior: 778k

Initial Jobless Claims 4-week ave. Forecast: - , Prior: 748.5k

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Continuing Jobless Claims Forecast: -, Prior: 6.071m

Retail Sales YoY (Oct) Forecast: 2.9%, Prior: 2.2%

ISM Services PMI (Nov) Forecast: 56, Prior: 56.6

Friday
12/4/2020

Factory Orders s.a. MoM (Oct) Forecast: 1.4%, Prior: 0.5%

Nonfarm Payrolls (Nov) Forecast: 520k, Prior: 638k

Unemployment Rate (Nov) Forecast: 6.8%, Prior: 6.9%

Factory Orders MoM (Oct) Forecast: 1%, Prior: 1.1%