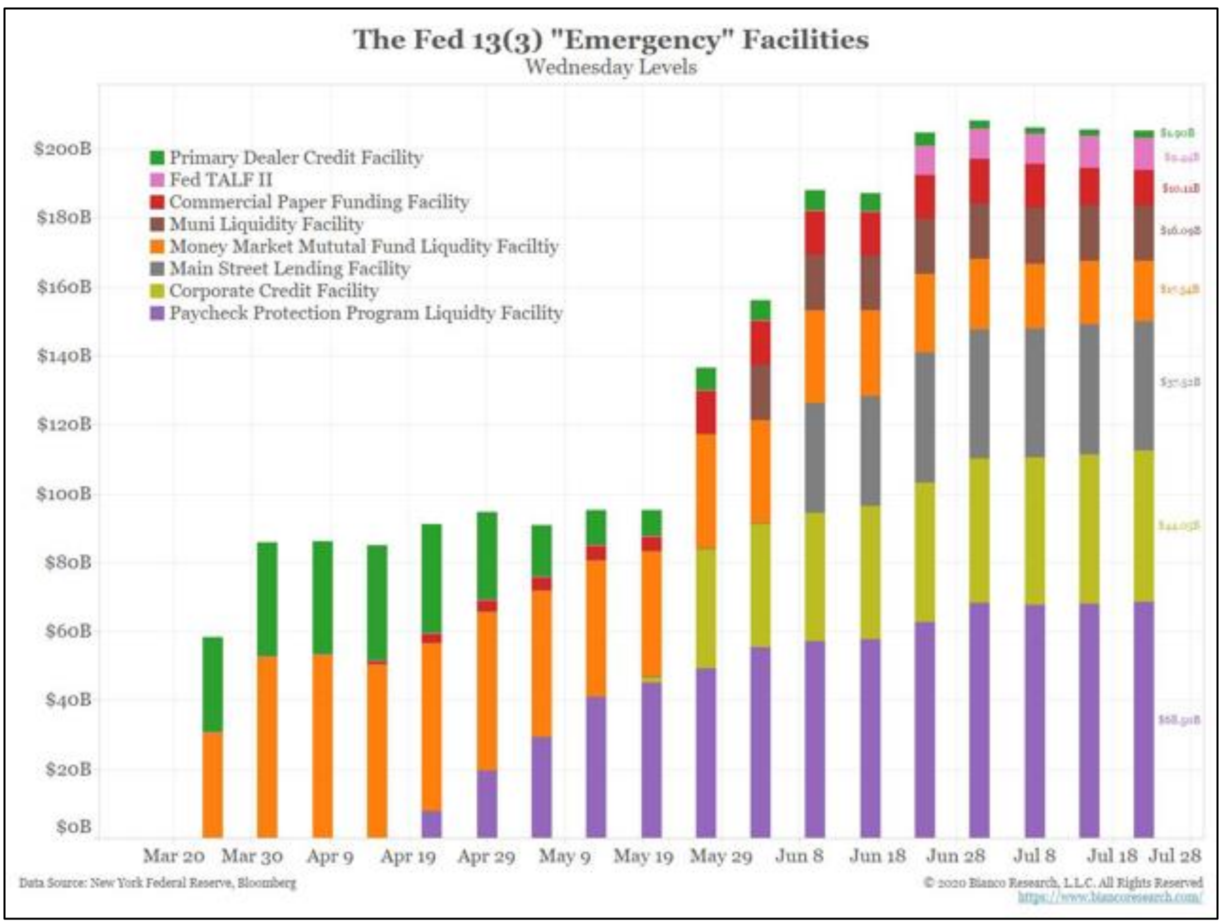
What to focus on in Global Macro for the week of July 27th, 2020

Macro Themes on the Radar:

Fed

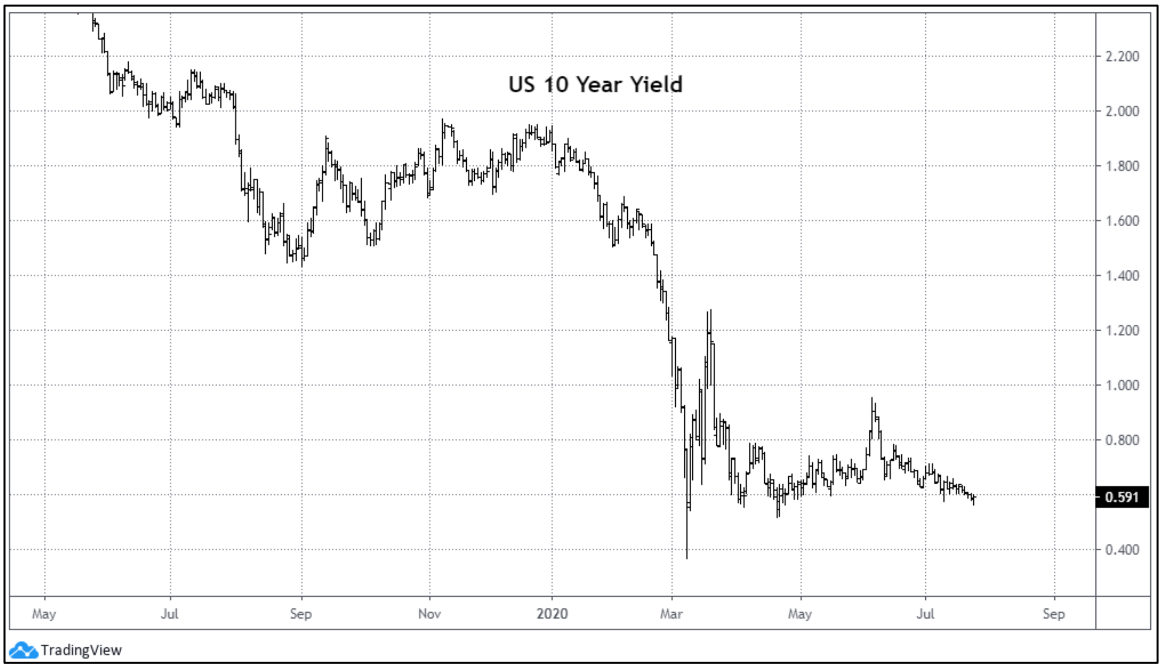
With this week's two-day meeting wrapping up on Wednesday, Fed watchers are contemplating what could come next. At least for now, negative rates seem to be off the table, so don't expect any rate changes. They could adjust QE in some way, maybe via a change in the mix of maturities and assets, but I don't expect much in that area either. They could further tweak the "emergency facilities"; which of course are really Treasury programs levered up via the Fed.

Here is a quick snapshot of what those Special Purpose Vehicle commitments currently look like.

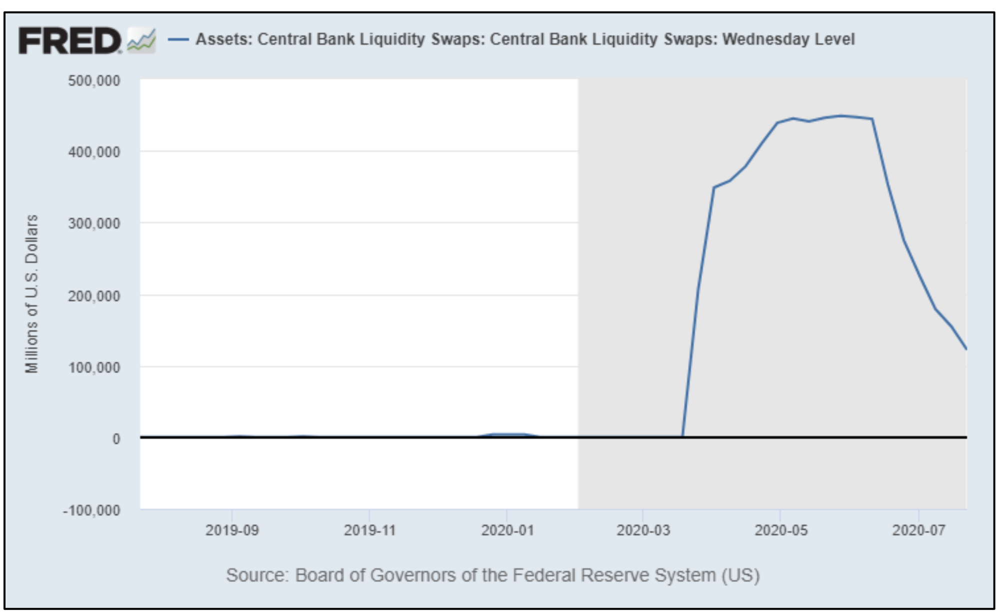


Source: Bianco Research

The most likely change is that they institute some form of explicit forward guidance about the future path of interest rates. Here they could tie future rate hikes to actual inflation outcomes (average inflation targeting), unemployment levels, or both. From the minutes, it became clear that this was discussed at length during the last meeting. There was little concern about strengthening forward guidance in some way, but also no agreement yet on what form that should take. Yield Curve Control is also still on the table but might be saved for later as they do more research. At least for now bond markets have been cowed by the Fed and global CB's, so there is no urgency to use this tool now. With so much uncertainty and internal reviews ongoing, any and all those policy decisions may wait until September or even the November meetings.



On the Fed's FX swap lines, they decreased another 33bln this week. The dollar shortage that we saw earlier in the year seems well controlled for now as total utilization is now at 122bln, down from a high of 449bln back in May.



COVID relief bill

This week we should get the GOP's version of the next round of COVID relief. The expectation is for an extension of the $600-a-week federal unemployment boost (maybe reduced but potentially until the end of the year) with the provision that recipients are capped from having unemployment benefits exceeding 70% of their previous salary. In addition, another $1,200 stimulus check has been promised, but potentially with a lower salary cap than last time.

EU

Although the EU Recovery Fund was agreed to by EU leaders, the EU budget (which the fund is part of) needs to be approved by the European Parliament. MEP's have already been voicing concerns and threatening to reject the EU's coronavirus budget. The lack of a rule of law mechanism is one issue. Another issue is the restoration of funding for some common projects that had been cut. Finally, some MEP's are seeking union-wide taxation to raise money for repayment of future bond issuance. Suggestions include taxes on tech companies, carbon emissions and even a supplementary VAT tax.

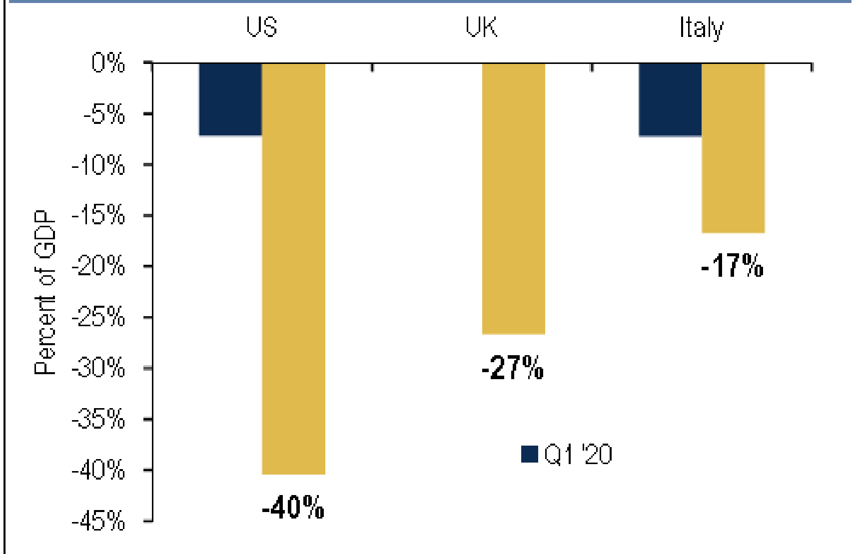
Germany's support for joint debt under the EU Recovery Fund has certainly been seen as a watershed event. It is unclear if the "frugals" see this as a one-off event or the breaking of a taboo. So far, I would guess the former. Inside Germany there is still plenty of uncertainty. Bundesbank President Jens Weidmann voiced his continued misgivings last week.

> *From a Reuters article:*
> *"It's important that the EU has proven its capability to act in the crisis," Weidmann told Funke media group in an interview, adding that showing solidarity also in financial terms was the right thing to do in the current crisis. But Weidmann added the agreed debt mechanism should remain an exemption and that strict conditions had to be attached to the financial aid. "Control mechanisms are needed to ensure that funds are used sensibly and efficiently," Weidmann said. "Generally, I think joint debt for extensive transfers is questionable. At the very least, the package should not serve as a springboard for large-scale EU debt for regular household financing," he said.*

What to Focus on Now:

Global monetary and fiscal expansion continues. With interest rate repression, government bonds are not seen as an effective hedge against the growing risk that inflation eventually starts to pick up.

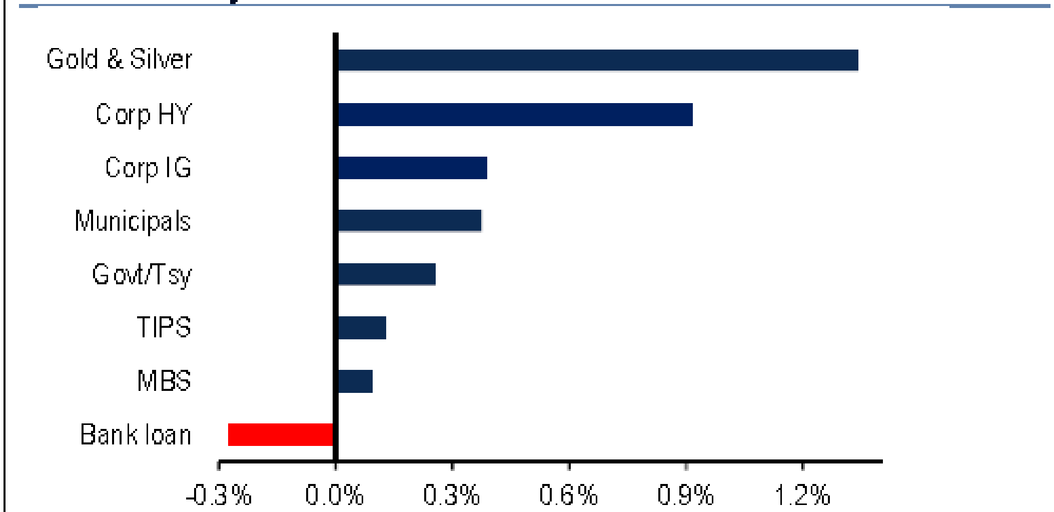
Chart 3: Q2'2020 US fiscal deficit hits 40% of GDP



Source: BofA Global Investment Strategy, Suttle Economics

Investors have been shorting USD and buying precious metals as a hedge against continued currency debasement.

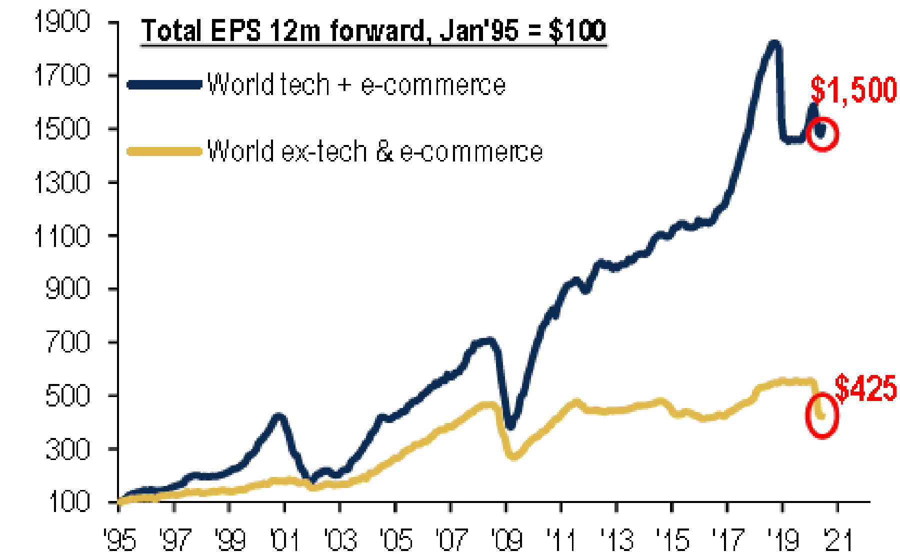
Chart 15: Weekly FICC flows as % AUM



Source: EPFR Global

However, a meaningful move to real assets and in favor of "value" vs. "growth" has barely started.

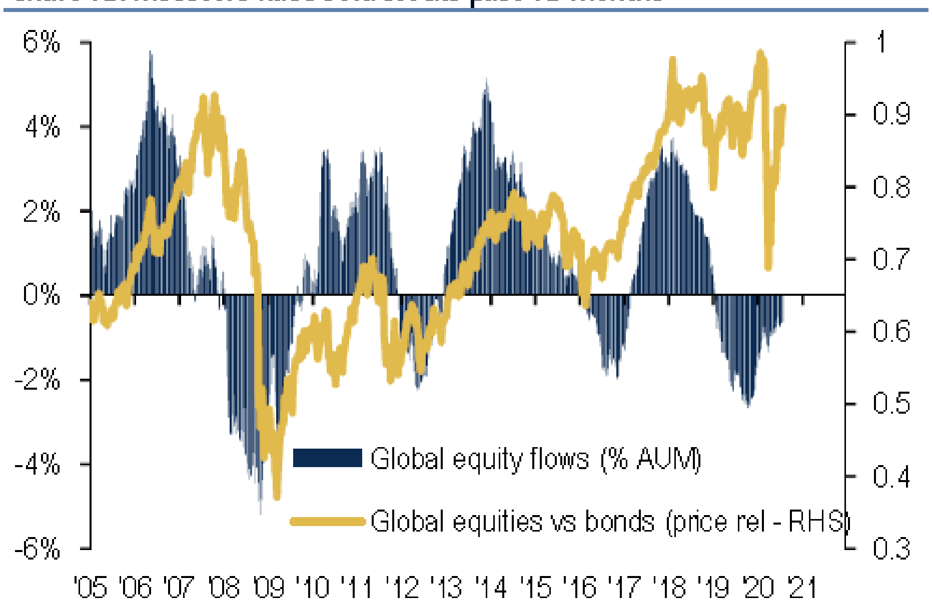
Chart 9: Deflation (credit & tech) dominating inflation



Source: BofA Global Investment Strategy, Datastream

The deflationary mindset is still powerful, and its legacy can be seen in the longer-term flows.

Chart 12: Investors have sold stocks past 12 months



Source: BofA Global Investment Strategy, EPFR Global; note 12 month cumulative flows

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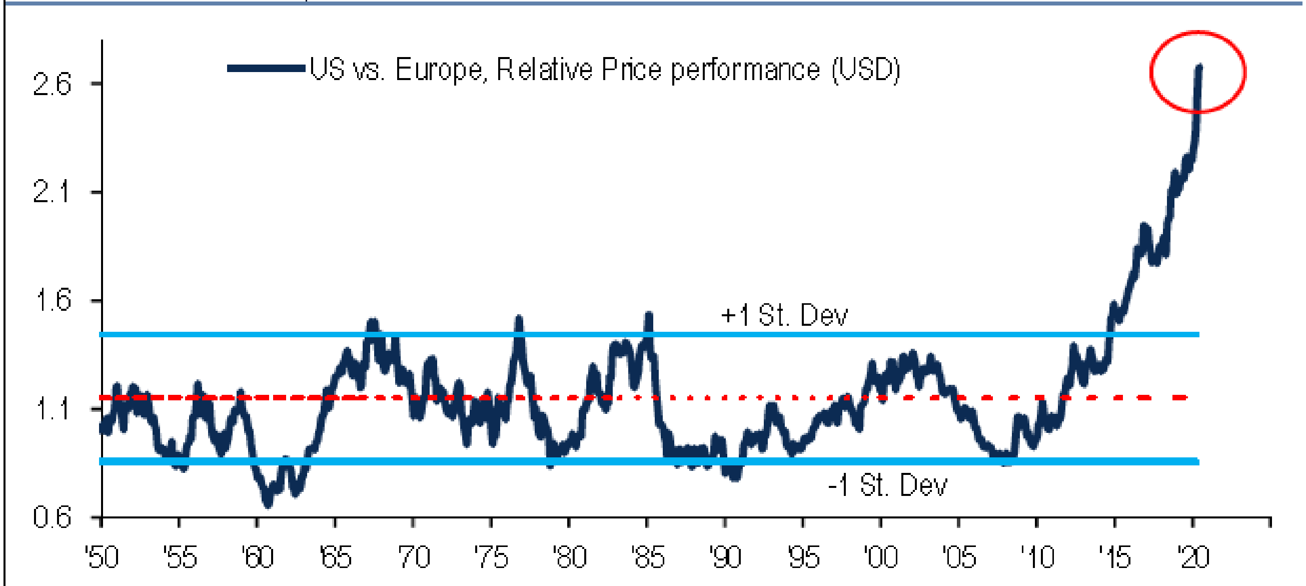
As discussed, the move into the "safe" US technology growth stocks has been THE driver of equities and US outperformance.

Chart 2: Global offence, American defense



Monthly data. GFD Europe index is used, which reconstitutes the MSCI Europe estimate pre-1970, and includes a 12% UK weighting until 1970, after which it uses actual MSCI Europe weightings; latest UK weight is approx. 26%
Source: BofA Global Investment Strategy, Global Financial Data, Bloomberg

Zoomed in, US outperformance has been sliding a bit, but no real turn confirmed yet via the S&P.

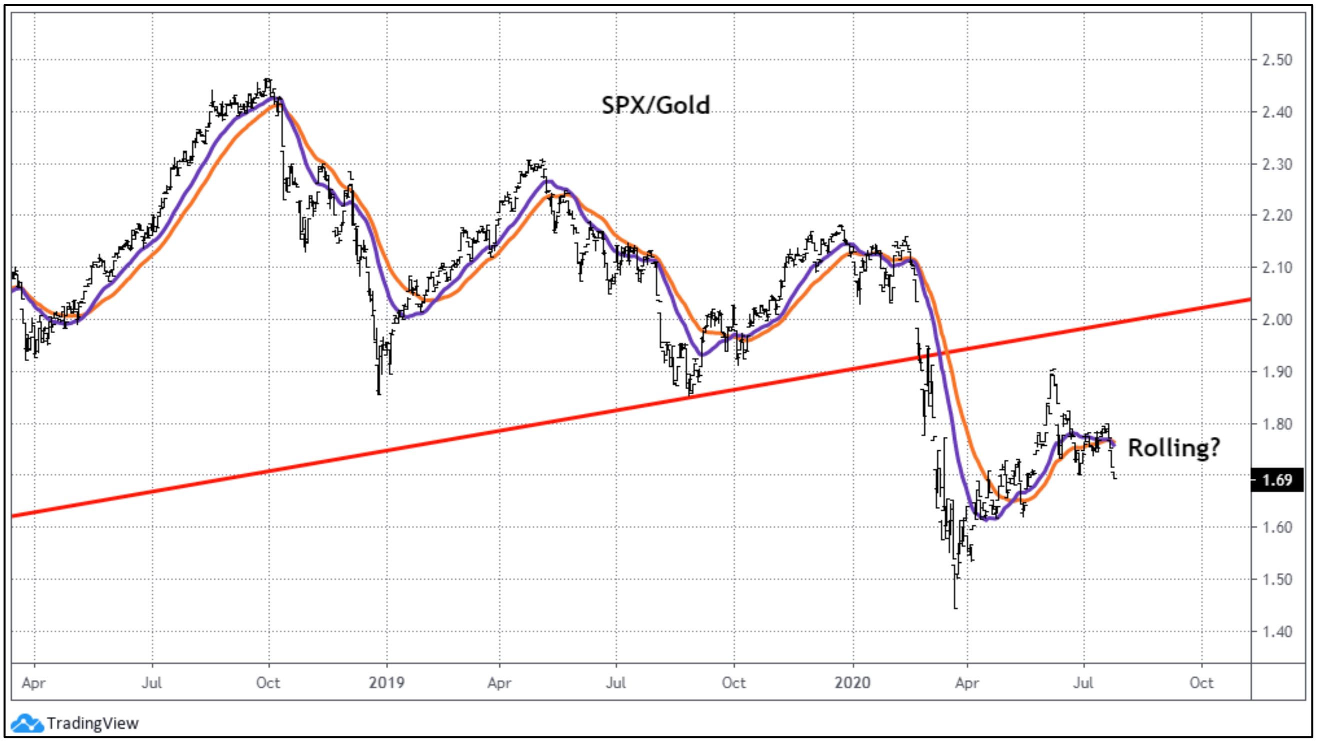
Against the more tech heavy NASDAQ however, the turn is potentially closer.

NASDAQ vs. Europe looks to be at an important point as well. This chart has higher volatility in the coming weeks written all over it…

Internally, US tech has had a meaningful reversal of its outperformance off the highs. I think we could see another 10% as high flying tech underperforms the Russell in the coming weeks.

Equities have not been able to keep up with the rallies in Gold and Silver. That's a big break in a long-standing trend.

With momentum rolling, further equity underperformance in the near-term is looking likely.



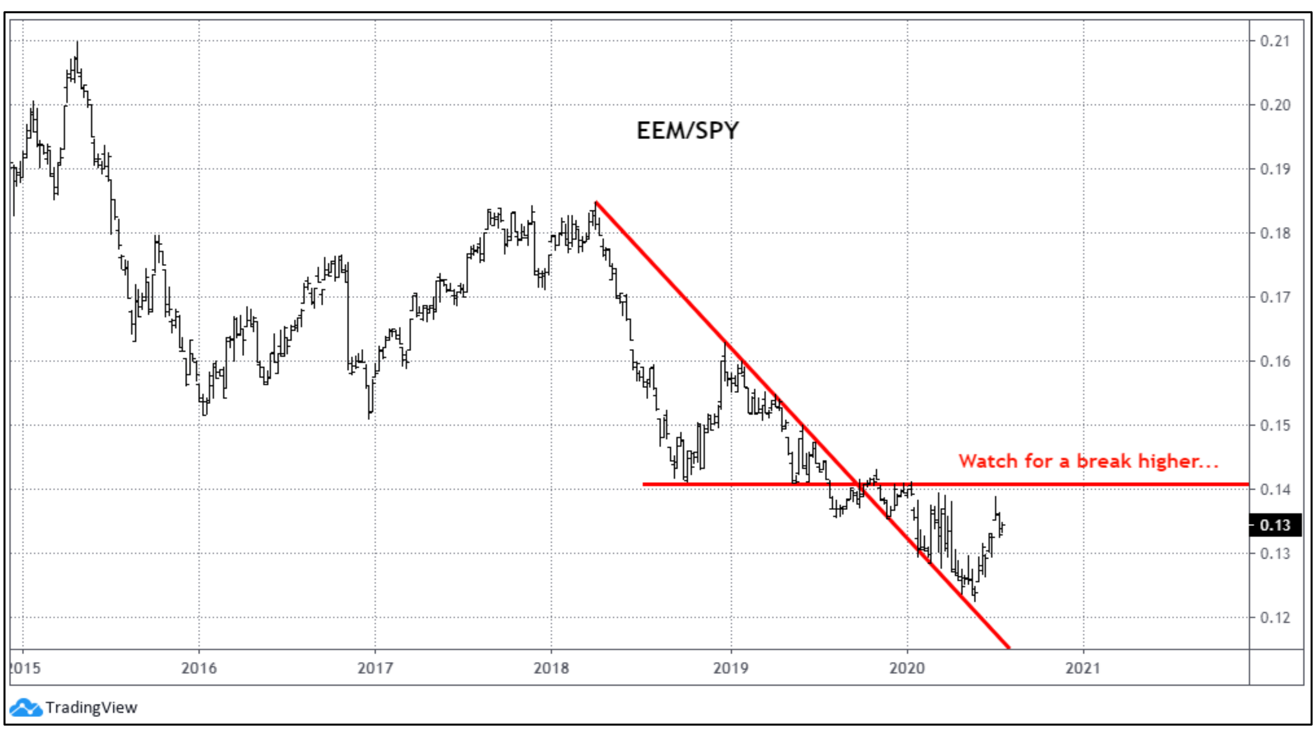
USD weakness will need to be part of that. There will be support as we approach 92.5 in the Dollar Index…

and equivalent resistance in EURUSD on a spike to 1.1800.

USDJPY cracked a big level on Friday. It will be interesting to see if we get any follow through this week. With FX vol still very low, USDJPY downside could be an interesting risk-off hedge.

Continuing the weak USD and relative performance themes, EM should benefit from a weaker USD. This would probably be predicated on a better global growth outlook rather than the USD falling in response to US specific concerns. In any case it is worth having on your radar.

There is a well-defined level to watch for EM outperformance…



Stargazer
Asset Management

Despite the EU deal, European equities don't look great. Momentum is lacking notwithstanding the potential catalyst we have had. There have been meaningful flows into Europe over the last 4-5 weeks and this "buy the rumor, sell the fact" price action is disappointing.

Germany is on support…

… as is France. Seems early for EUR currency strength to be causing any misgivings. This needs to be watched for risk management on outright long positions.

Final note … is Silver just getting started?

Stargazer
Asset Management

Important Macro Data Releases and Events for the Week

Monday 7/27/2020	IFO - Business Climate (Jul) Forecast: 89.3, Prior: 86.2
	IFO - Current Assessment (Jul) Forecast: 85, Prior: 81.3
	IFO - Expectations (Jul) Forecast: 93.4, Prior: 91.4
	Durable Goods Orders ex Trans (Jun) Forecast: 3.5%, Prior: 3.7%
	Durable Goods Orders ex Defense (Jun) Forecast: 18.6%, Prior: 15.3%
	Durable Goods Orders (Jun) Forecast: 6.5%, Prior: 15.7%
	Nondefense Capital Goods Orders ex-Aircraft (Jun) Forecast: 1.5%, Prior: 1.6%
Tuesday 7/28/2020	S&P/Case-Shiller Home Price Indices YoY (May) Forecast: 4%, Prior: 4%
	US Consumer Confidence Forecast: 94.5, Prior: 98.1
Wednesday 7/29/2020	**FOMC Interest Rate Decision/Monetary Policy Statement/Press Conf.**
Thursday 7/30/2020	GDP QoQ (Q2) Forecast: -9%, Prior: -2.2%
	Unemployment Change (Jul) Forecast: 45k, Prior: 69k
	Economic Bulletin REPORT
	Consumer Confidence (Jul) Forecast: -15, Prior:
	Harmonized Index of Consumer Prices YoY (Jul) Forecast: 0.4%, Prior: 0.8%
	Personal Consumption Expenditures QoQ (Q2) Forecast: 1.6%, Prior: 1.3%
	Core Personal Consumption Expenditures QoQ (Q2) Forecast: 1.7%, Prior: 1.7%

- Initial Jobless Claims Forecast: 1.4m, Prior: 1.416m
- Initial Jobless Claims 4-week ave. Forecast: - , Prior: 1.36025m
- Continuing Jobless Claims Forecast: -, Prior: 16.197m
- GDP Price Index (Q2) Forecast: 1.2%, Prior: 1.6%
- GDP Annualized (Q2) Forecast: -35%, Prior: -5%

Friday
7/31/2020

- NBS Manufacturing PMI (Jul) Forecast: 51, Prior: 50.9
- Non-Manufacturing PMI (Jul) Forecast: 51.2, Prior: 54.4
- Retail Sales YoY (Jun) Forecast: 1.4%, Prior: 3.8%
- CPI Forecast: 0.2% and Core Forecast: 0.7%
- GDP QoQ (Q2) Forecast: -12% and YoY (Q2) Forecast: -14.1%
- Personal Income Forecast: -0.2%, Prior: -4.2%
- Personal Spending Forecast: 5%, Prior: 8.2%
- Chicago PMI (Jul) Forecast: 43, Prior: 36.6
- Michigan Consumer Sentiment Index (Jul) Forecast: 72.8, Prior: 73.2

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