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What to focus on in Global Macro for the week of May 3rd, 2021

Macro Themes on the Radar:

As expected, the Fed meeting was pretty uneventful. They upgraded their view of the economy and indicated that the recovery was progressing faster than previously expected, but that "it remains uneven and far from complete" and "a long way from our goals." Inflation was likely to continue higher in the near term, but would be transitory and due to base effects, and short-term demand and supply mismatches because of COVID. With regard to tapering asset purchases, "it is not time" for that conversation, and that "substantial further progress" is needed. Seems he really meant the "progress" bit as he reportedly said it 13 times during the press conference. When asked about high asset prices he said, "I won't say it has nothing to do with monetary policy, but also it has a tremendous amount to do with vaccination, and reopening of the economy, that's really what has been moving markets a lot in the last few months". For the first time acknowledged that "some of the asset prices are high" and that parts of the market "are a bit frothy, and that's a fact."

On Friday, Dallas Fed's Kaplan (not a voting member currently and generally hawkish) had a very different view, which arguably elicited more of a reaction from the markets than the FOMC meeting itself. Stocks got hit and USD went bid.

He said, "we're now at a point where I'm observing excess and imbalances in financial markets." With "historically" elevated stock prices, tight credit spreads, and surging house prices. "I do think, at the earliest opportunity, I think it would be appropriate for us to start talking about adjusting those purchases." Markets didn't like this taper talk just two days after being told by Powell that all is well. Kaplan doesn't get to make the call, but others may start having similar thoughts.

Also, the Bank of Canada's recent move to taper is fresh in people's minds. With a lot of central bank policy meetings coming up over the next few weeks, investors will be looking to see if others follow the BoC's lead.

Investors have a lot of moving parts to deal with now as they ponder when the Fed will start pulling back accommodation, how the inflation story will develop, when things like ISM and PMI's will top, and how much of the Biden spending and tax hikes with actually be enacted.

This Friday's US employment numbers could be big again. Don't be shocked if we break +1 mln. That would be another entry in Powell's "string" of large employment gains required to initiate the taper process.

After last week's numbers we are now nearly back at pre-COVID GDP.

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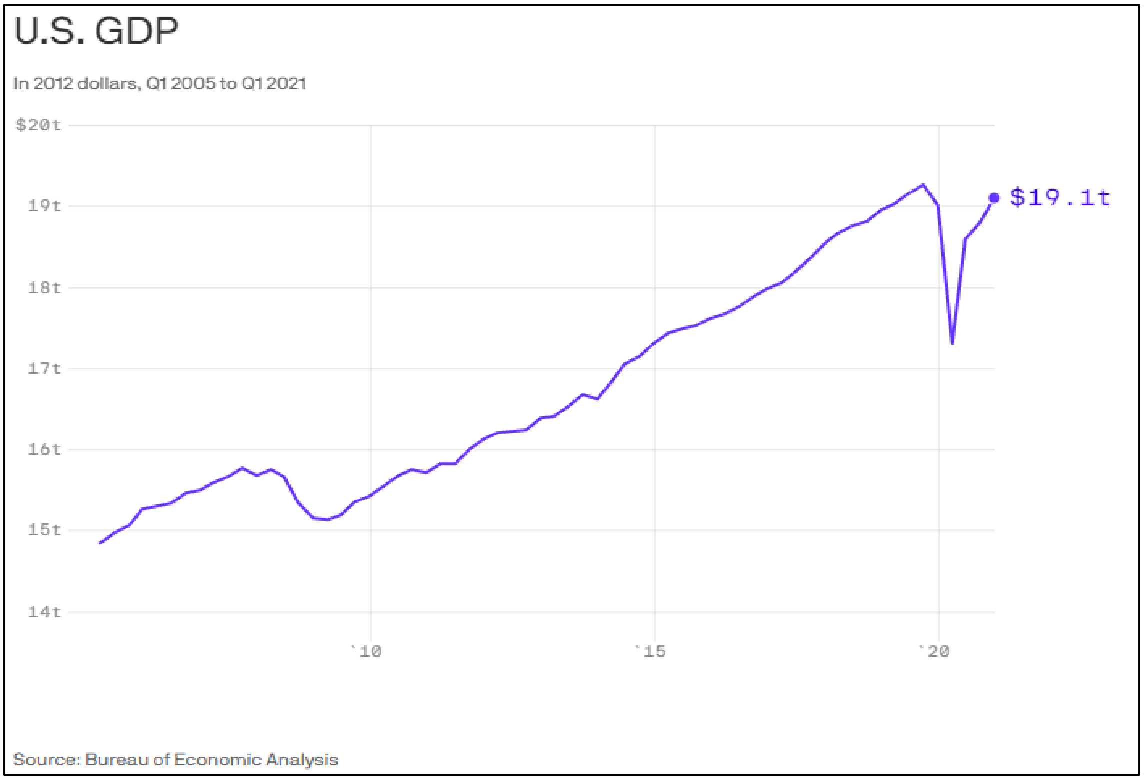
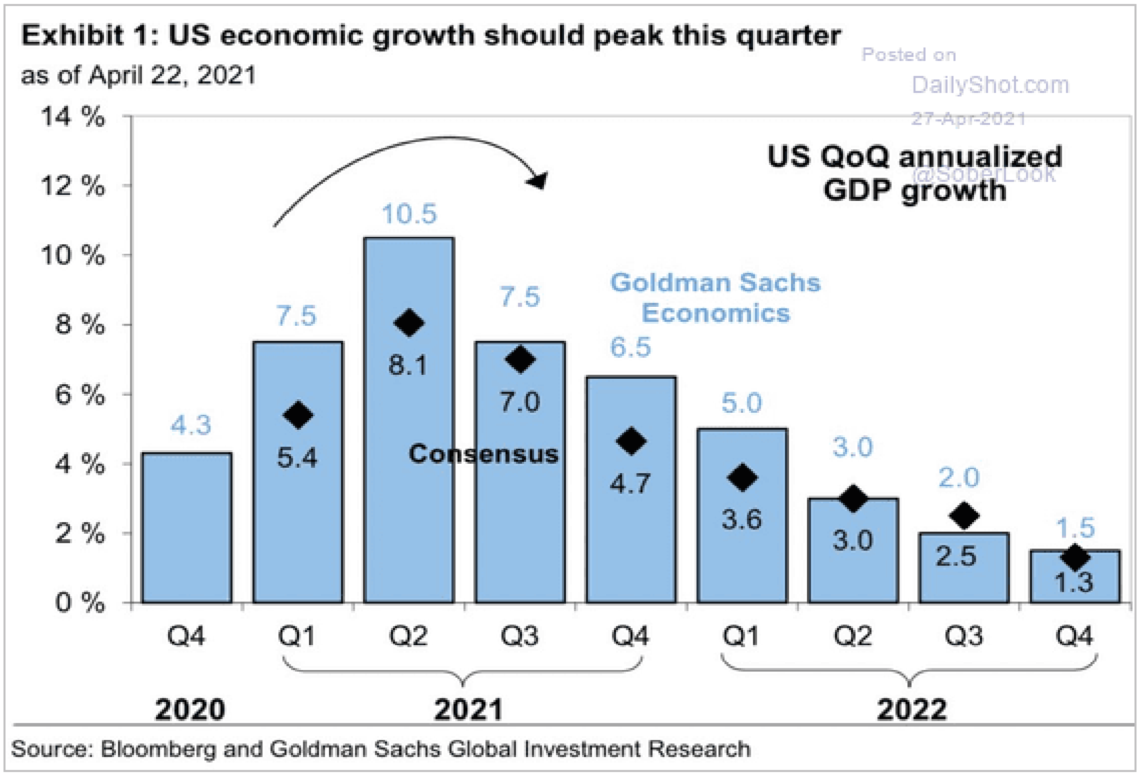
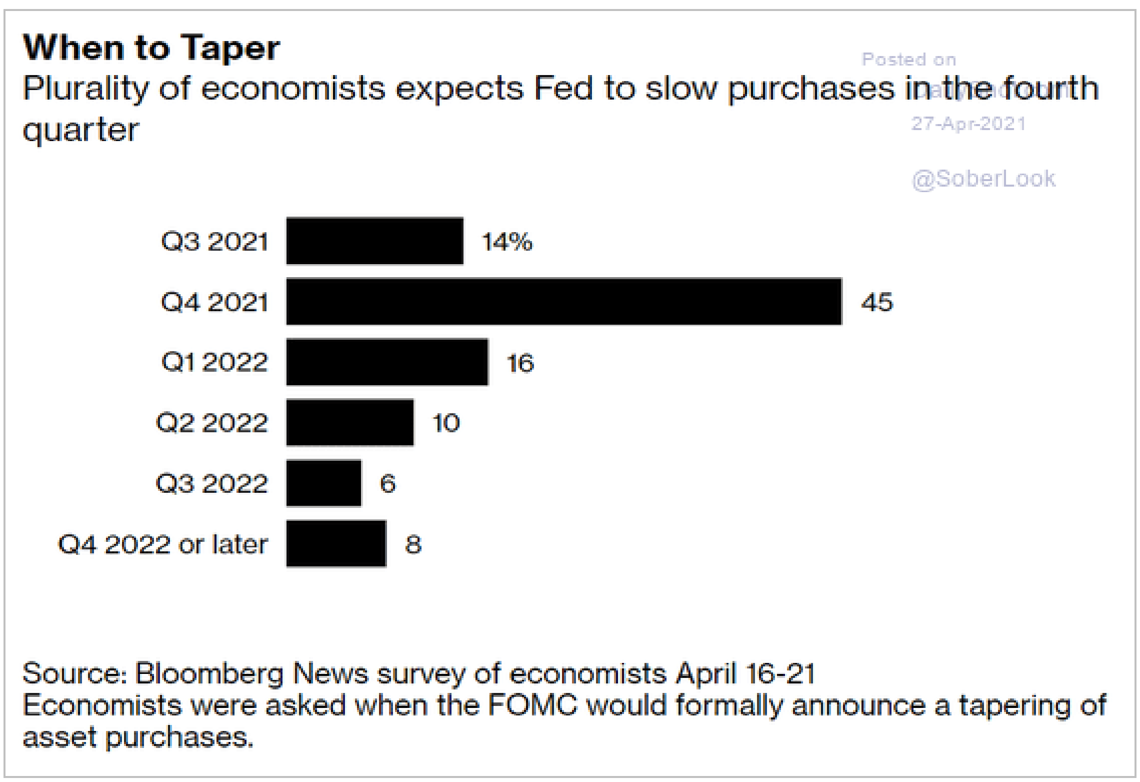


Inflation is on everyone's mind … "inflation" mentions on earnings calls.

While growth should stay strong all year, Q2 likely sees the peak. ISM and PMI's will top soon.



No doubt in my mind that taper will be a topic at the June FOMC meeting.



What to Focus on Now:
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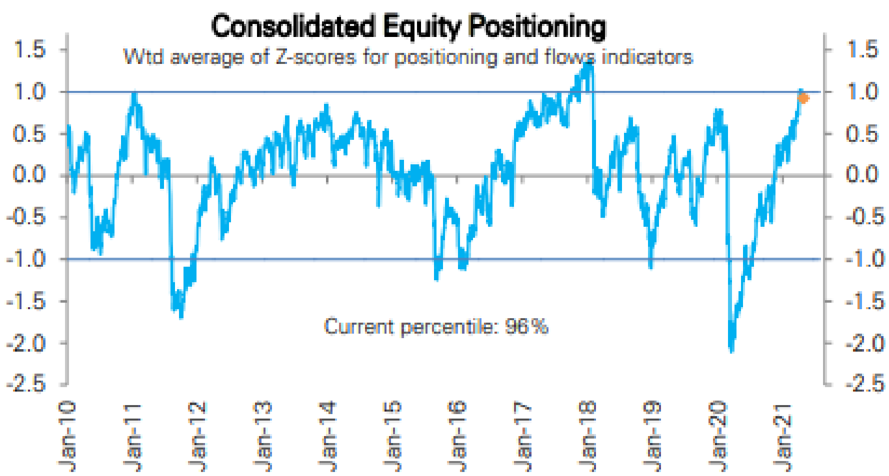
Equities

With the massive inflows over the last few months, investors are clearly long stocks now.

Figure 1: Consolidated equity positioning[1]

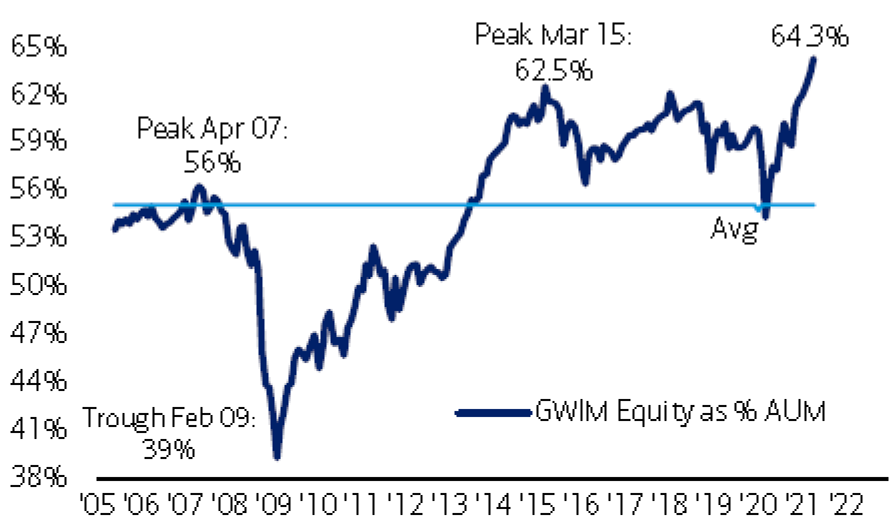


*Weights based on explanatory power in regression of equity performance on indicators

Source : EPFR, CFTC, Bloomberg Finance LP, Haver, Deutsche Bank Asset Allocation

Chart 16: GWIM equity allocation hits another new high at 64.3%

BofA private client equity holdings as % of AUM



Source: BofA Securities

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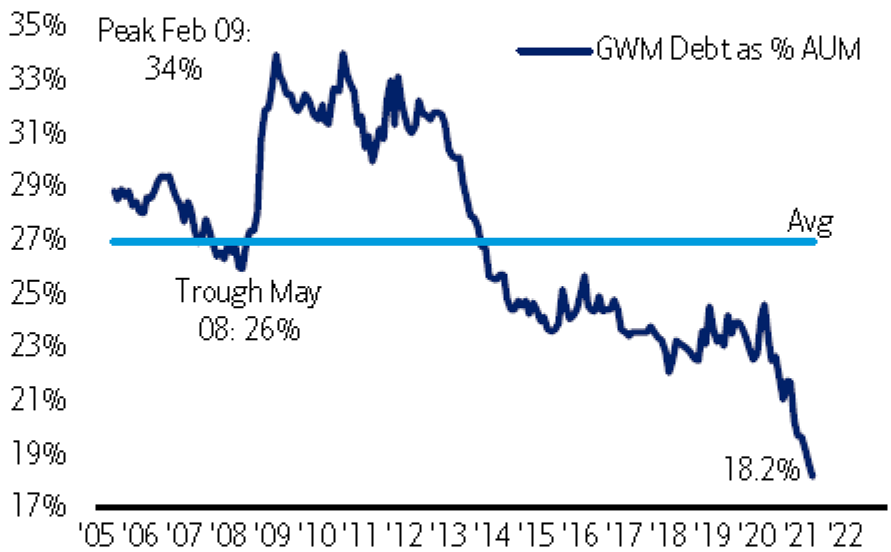
According to BoA, private wealth clients are now also positioned for higher inflation. They have been lightening up further on debt and increasing exposure to global growth and inflation.

Chart 17: GWIM debt allocation sinks to a new low at 18.2%

BofA private client debt holdings as % of AUM



Source: BofA Securities

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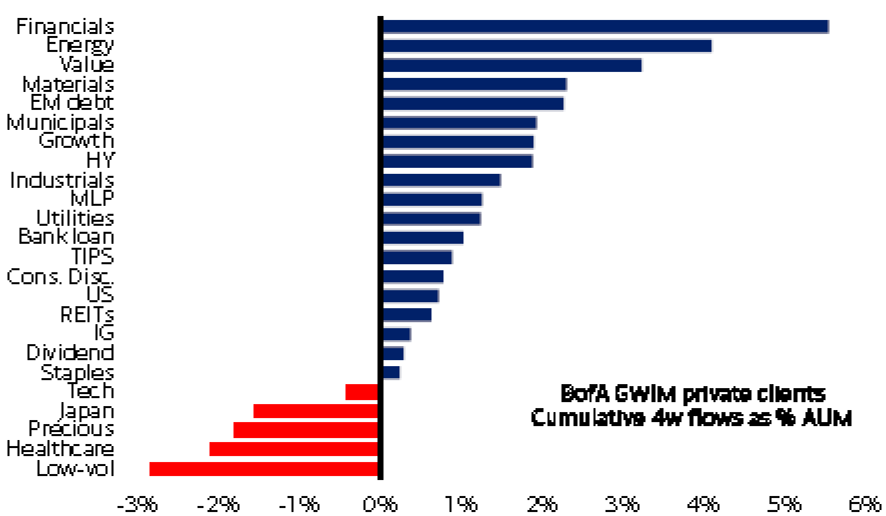
Chart 15: GWIM flows have favored financials, energy, value

BofA private client 4-week ETF flows as % of AUM



Source: BofA Securities

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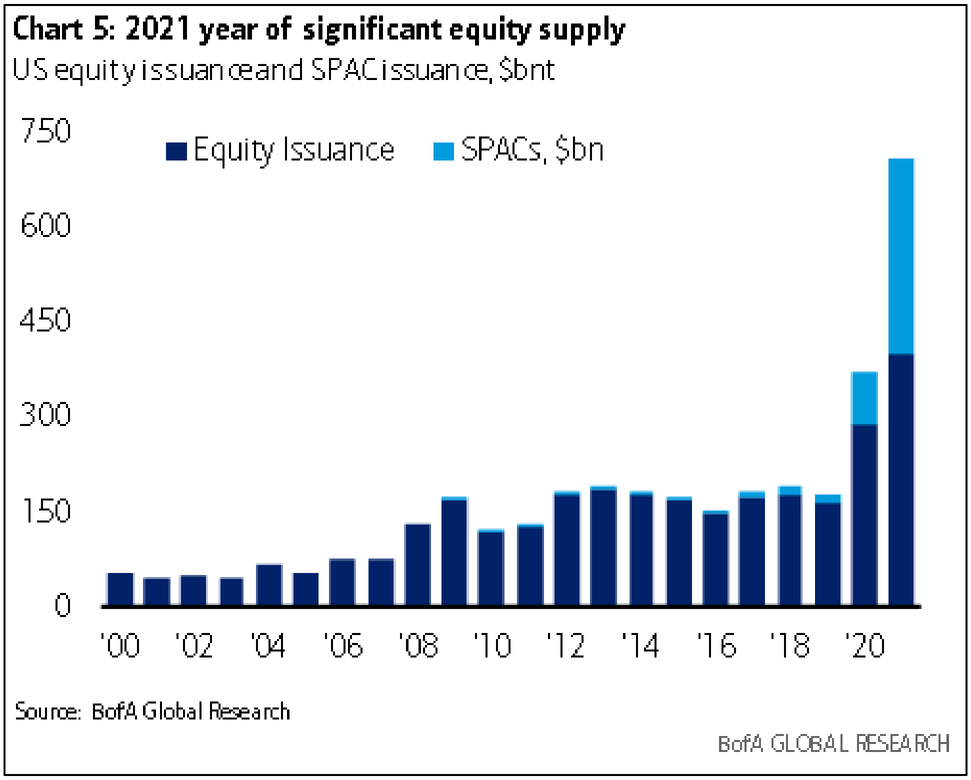
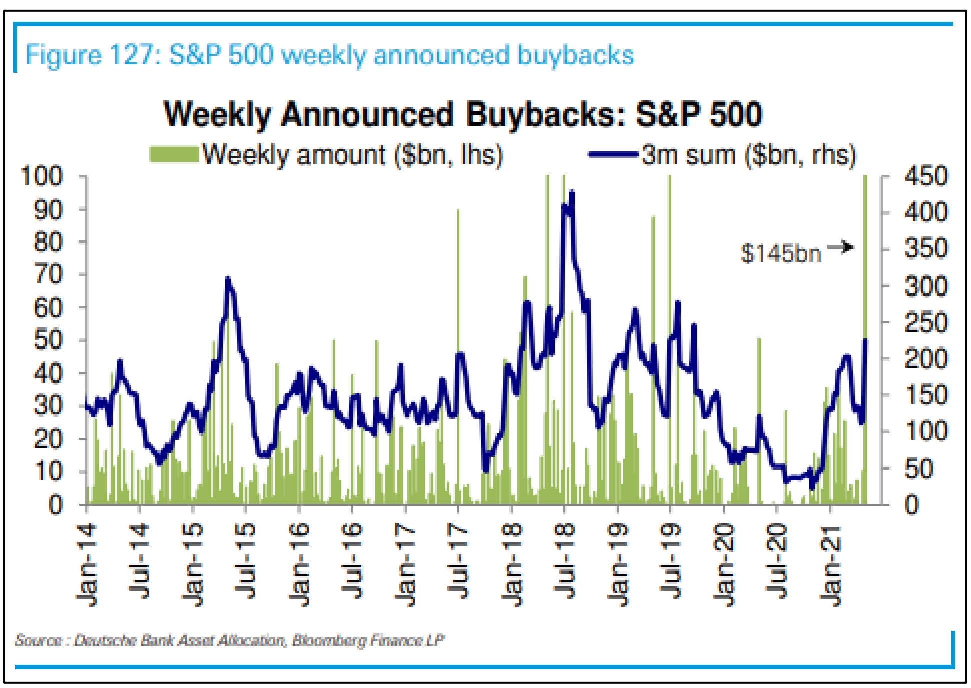
There has been a lot of talk about all the issuance and what happens when the lockups expire…



At least some of that looks like it will be counteracted by the new rush to increase buybacks.



While Friday's price action was a bit ugly, overall, April was a very good month for US equities. Short-term, however, there is some loss of momentum, and I could see a soft patch developing.

Europe, having failed to make any progress over the last few weeks, has a similar issue.

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Japan has also stalled... but is holding up so far.

China is the worst of the bunch and a little worrisome, but also has some idiosyncrasies.

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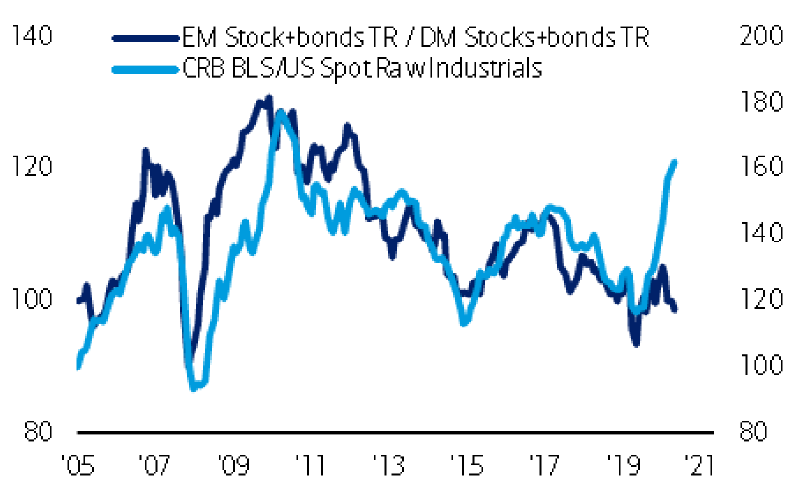
There has been a broadening, and now far-reaching, antitrust crackdown by the Chinese government. In addition, PMI's have been coming in a bit softer than expected

EEM has not been trading well. Certainly, the China exposure isn't helping, but the issue is bigger than that. COVID continued to ravage various EM countries as unsynchronized waves hit country after country. Brazil has been a horror show, now of course India.

Chart 8: ...nor EM assets reflect strength of commodities
EM vs DM stock and bond total return vs Commodities



Source: BofA Global Investment Strategy, Bloomberg

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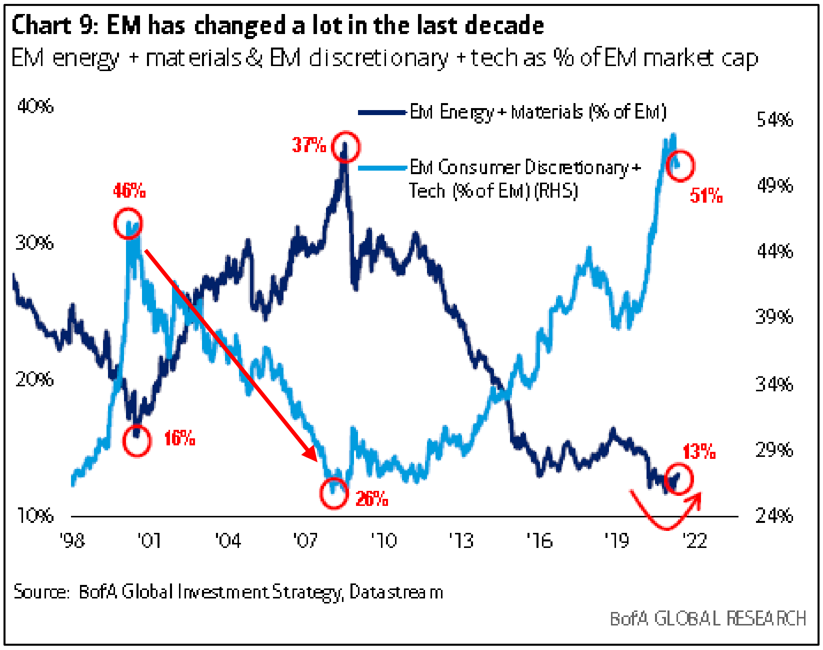
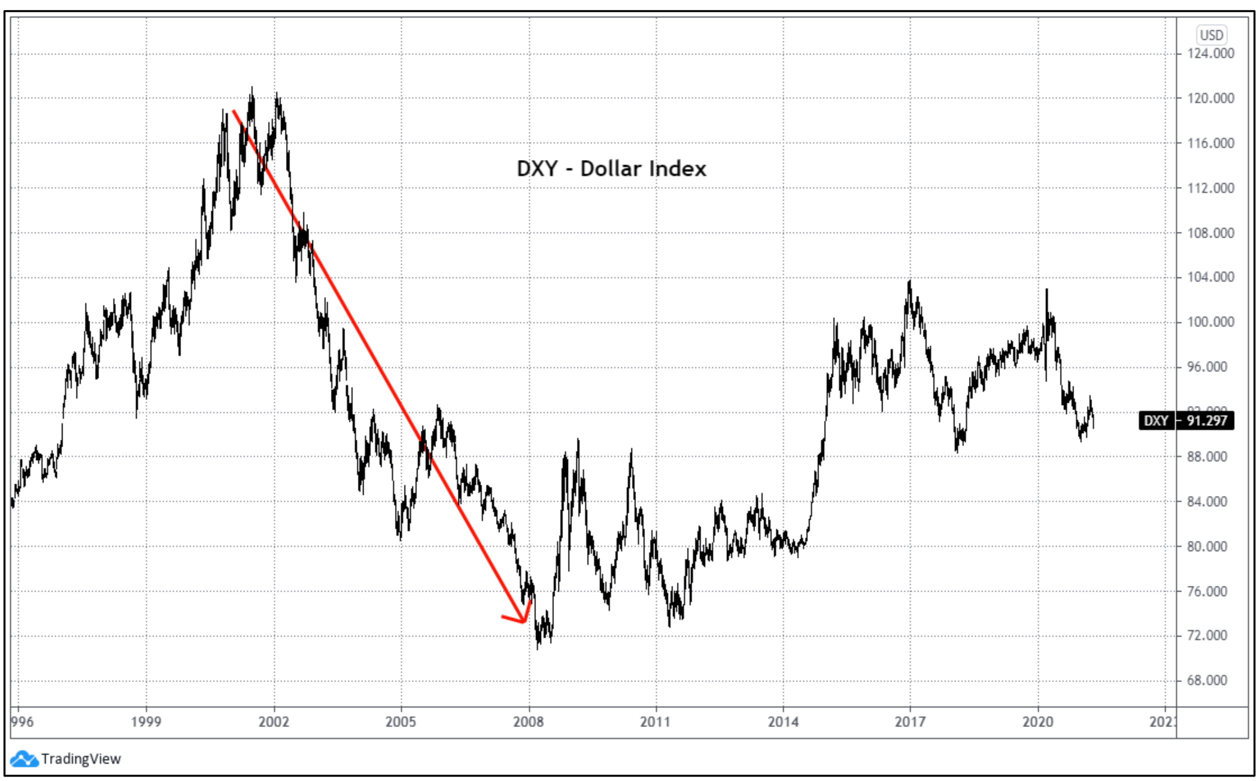
This may explain why EM assets in general have not performed as well during this commodity run as you would expect given historical precedent.

It probably also speaks to the bout of deglobalization we are seeing and the expectations that the current run in commodities is at least partially unsustainable and due to COVID and its lockdown and reopening effects.

BoA points out that EM has changed a lot in terms of the percentage makeup of the market cap. I would say fair enough point. But that it can quickly reverse if we get a continued USD selloff as that would trigger a virtuous cycle for EM and commodities.



So far this move in commodities has not really been powered by a falling USD, but by actual supply constraints. Notice the red lines in the above and below charts.



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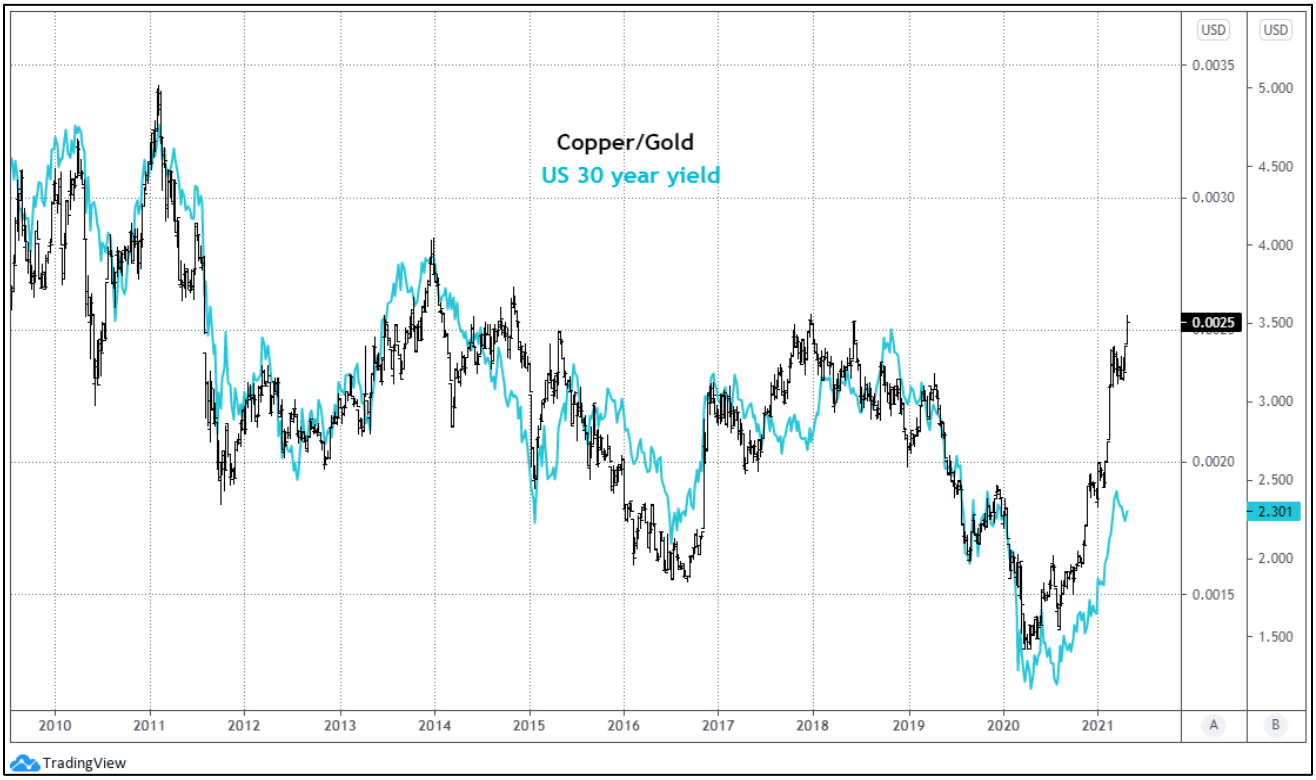
Bonds and Commodities

While bond yields have certainly risen as the economy rebounds (reflation), however, they have not yet bought into the booming inflation story.



With commodity prices going crazy and M2 through the roof, you can certainly see why inflation expectations have jumped.

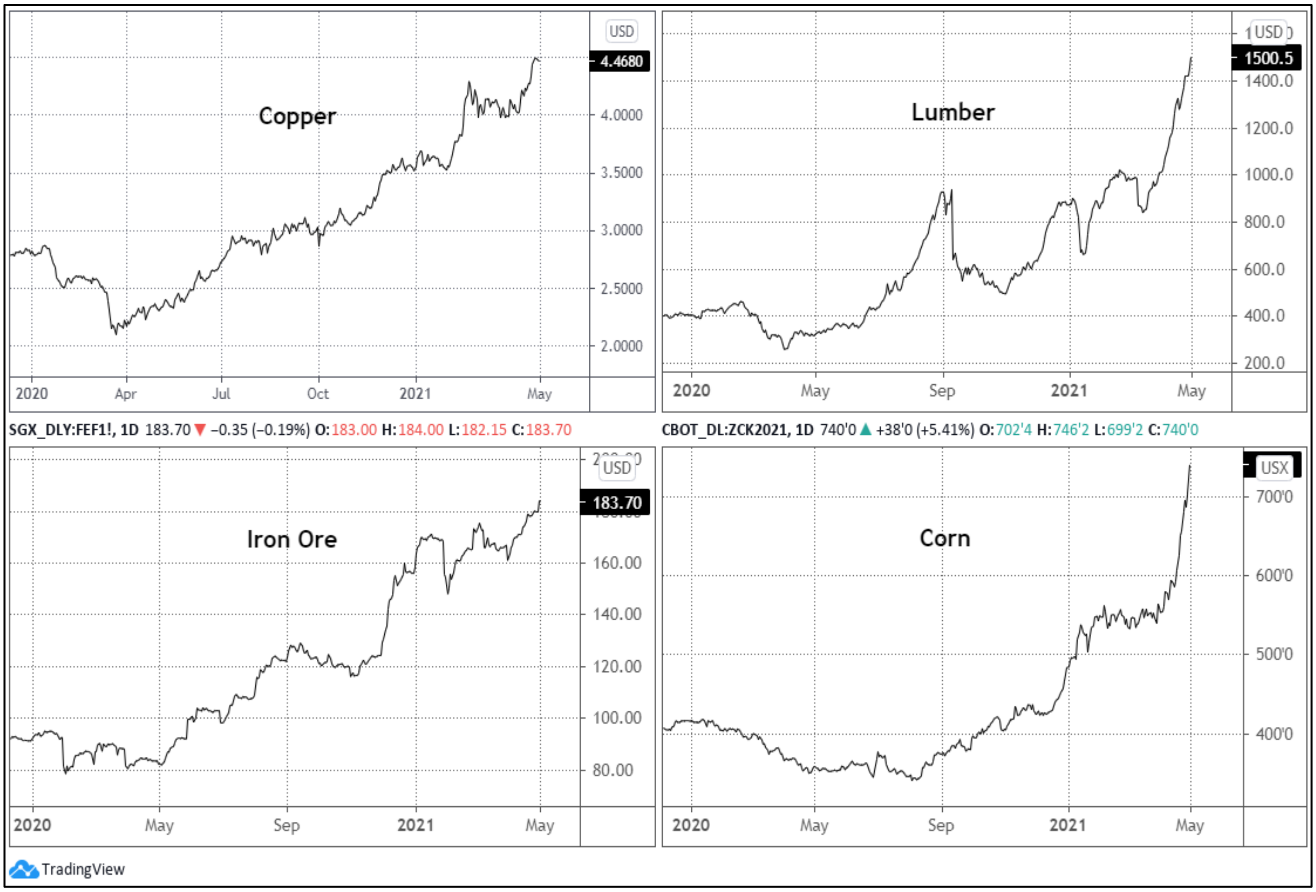
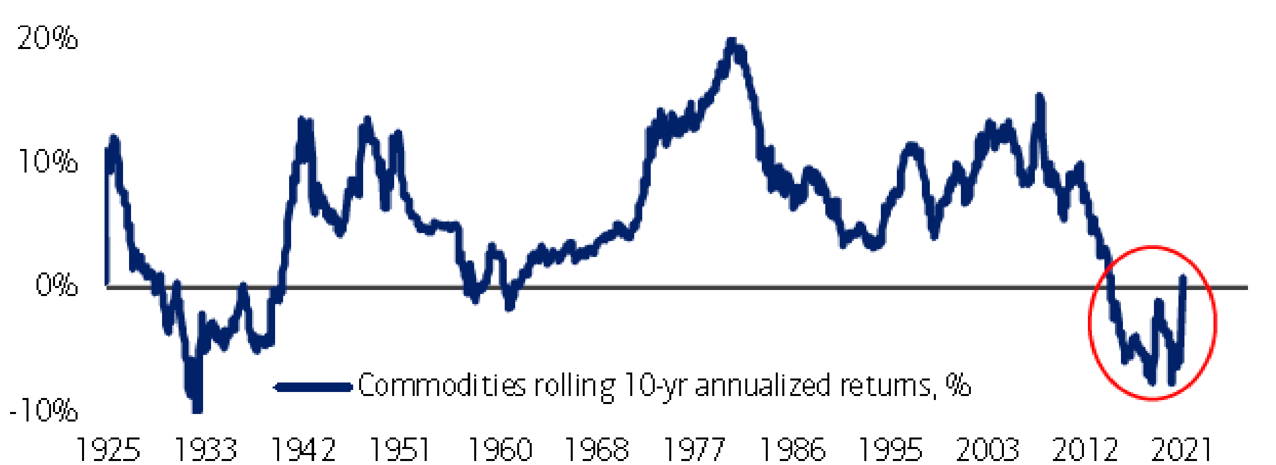


Chart 2: 10-year rolling return from commodities now positive for 1st time since 2014

Commodities rolling 10-year annualized returns, %



Source: BofA Global Investment Strategy, Global Financial Data

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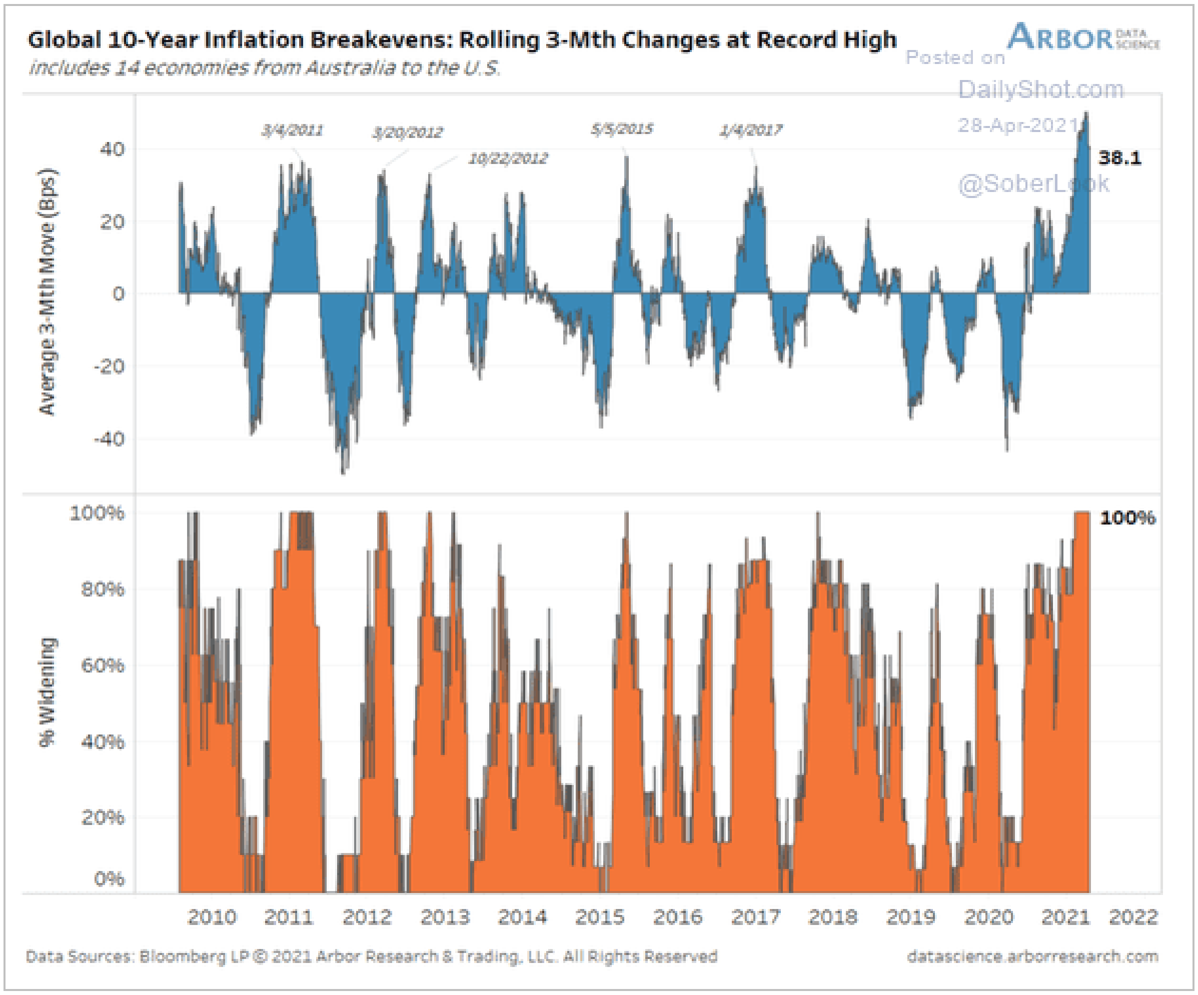
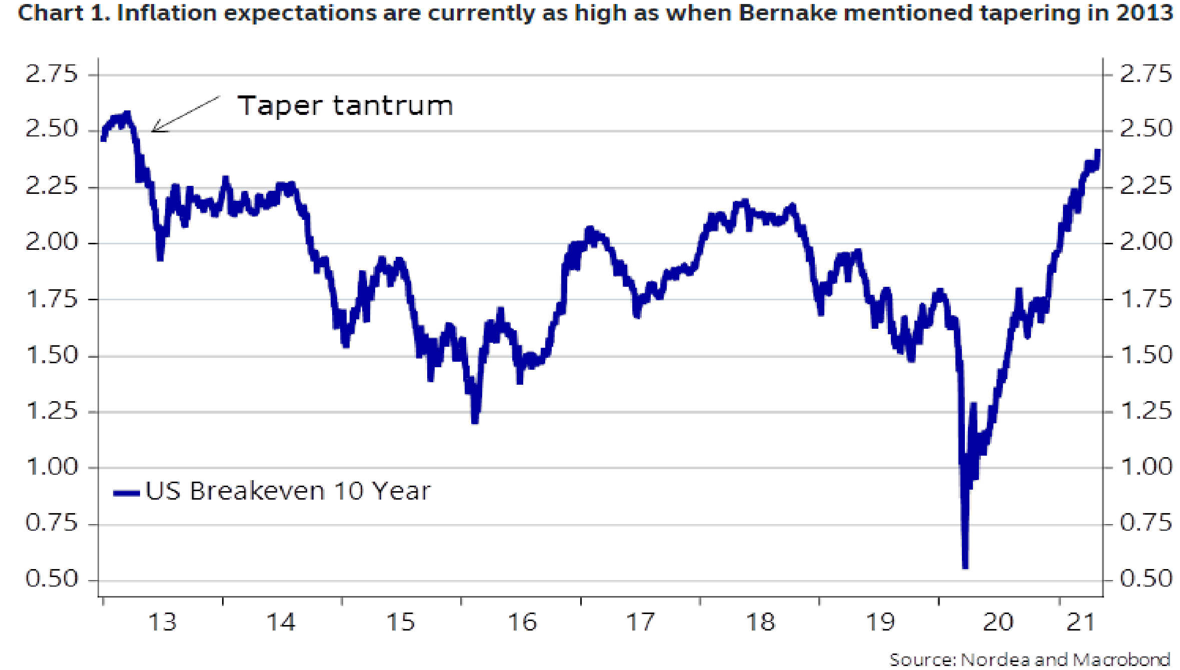
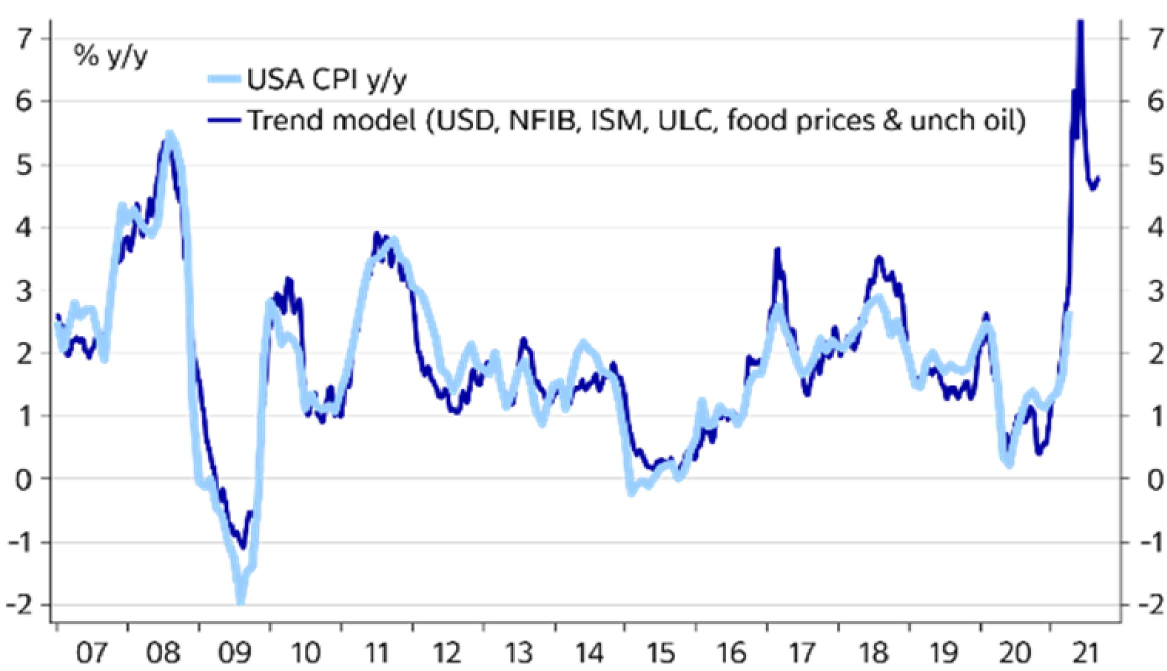


Chart 1. Inflation expectations are currently as high as when Bernake mentioned tapering in 2013



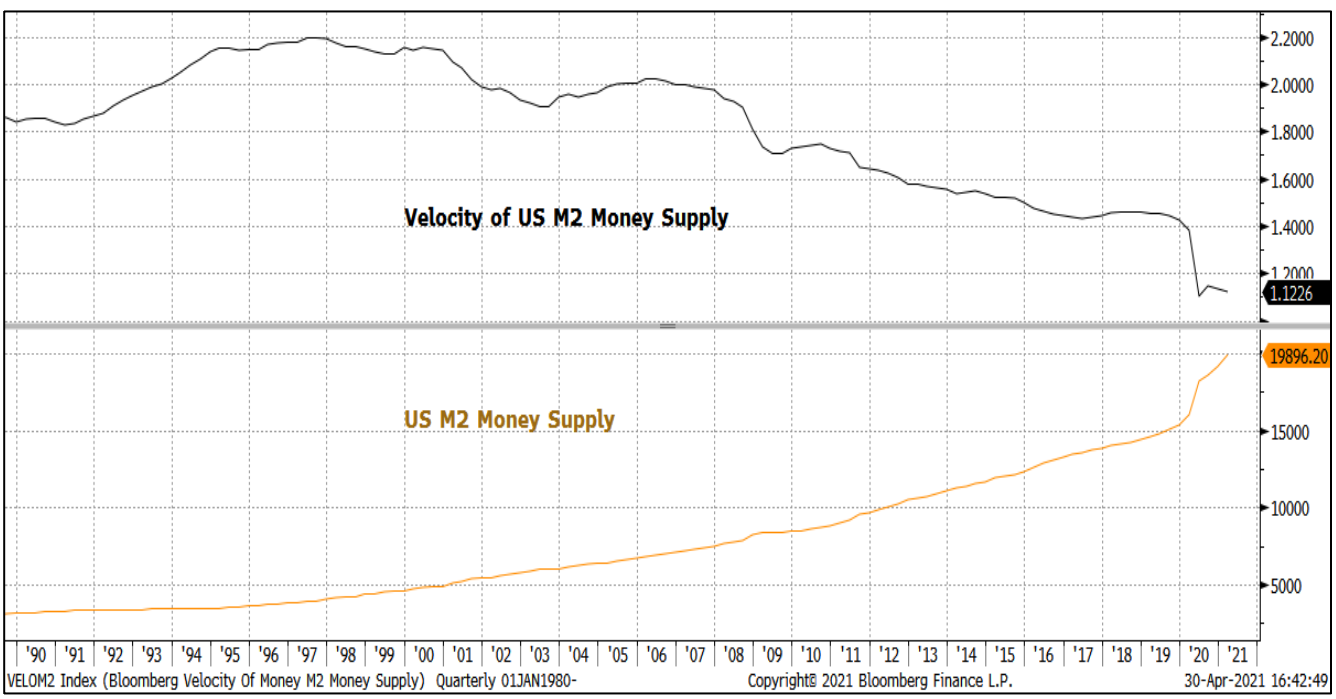
Some of the inflation models are very dramatic (hard to believe) because of the COVID induced extremes. However, even a jump to 4% would mean a collision between the Fed framework and market expectations. Transient or not, that would be volatility-inducing stuff.

Chart 9. Our inflation model is summoning its inner doom monger

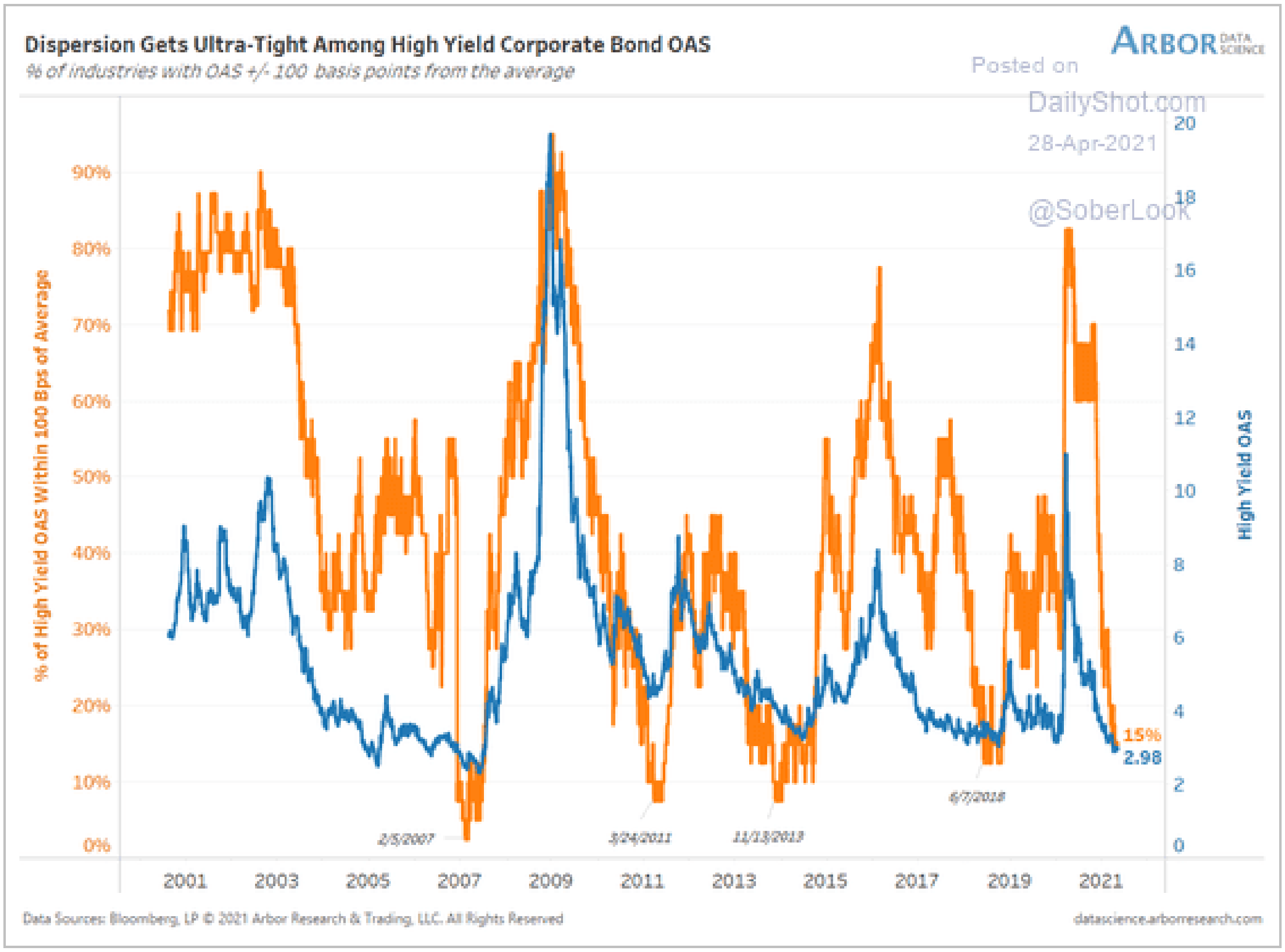


Source: Macrobond and Nordea

Will the velocity of money now pick up with full re-opening?



Credit spreads have been very tight and moving together. The draw of some yield during strong economic growth has been too much to pass up. I'll bet there are a lot of tourists in this asset class now that could be taught a hard lesson if yields jump and the markets get destabilized. This is a space well worth watching.



FX

Currencies have been tricky and for the most part without a good trend. This isn't making Macro traders happy by any means. The dollar had an interesting run vs. JPY and CHF as us yields were rising, but now with the bond move on hold that too has calmed down. CAD and NOK have been strong with good growth stories and the link to oil but otherwise, it has been slim pickings. As a result, implied volatility is very low. I think the low vol will provide an opportunity in the coming months.

For all the fuss, and a few ups and downs, the EUR is very close to where it was at the end of August.

The dollar is caught here between opposing forces. On one hand, huge government spending, loose monetary policy, and a big trade deficit should be pushing it lower. On the other hand, economic outperformance, partly due to the very same government spending (and a much better vaccine rollout), is making the US attractive. How this is resolved will have a huge impact on global asset allocation. The bear case…

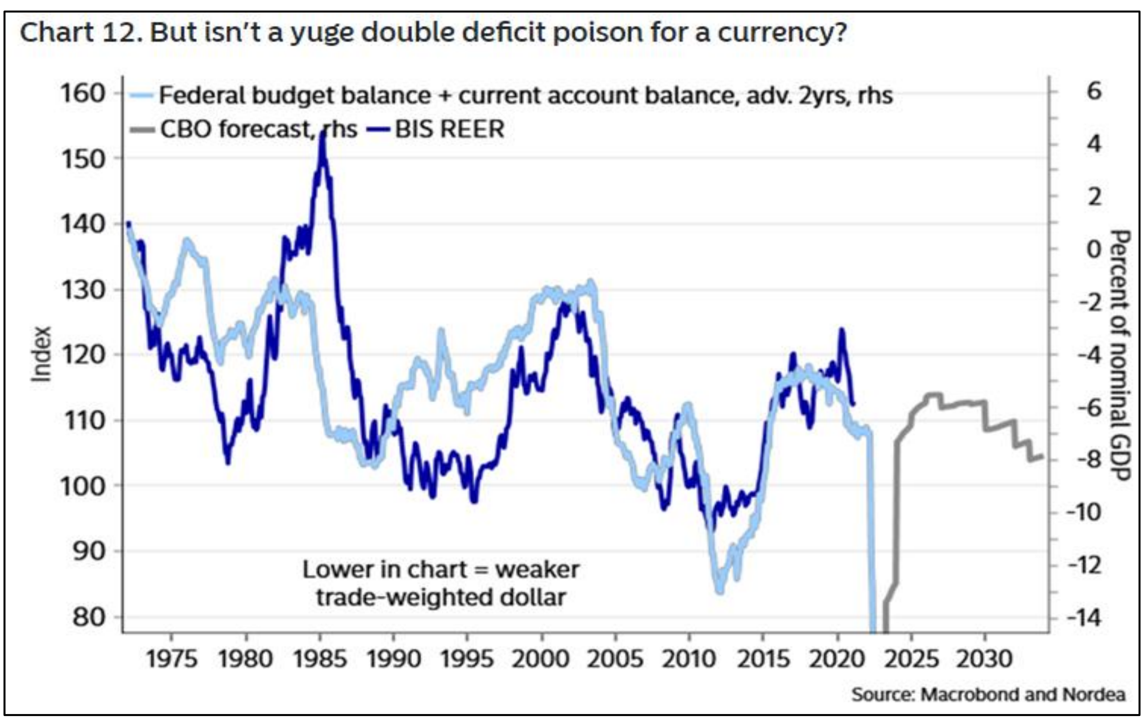
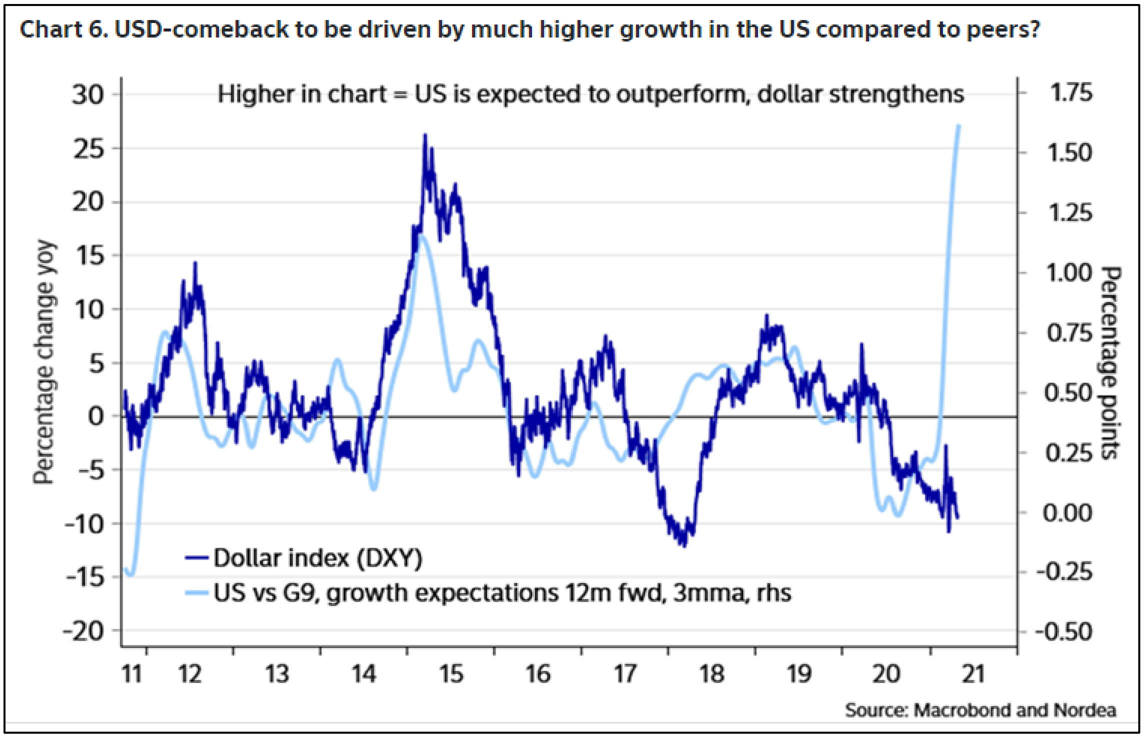


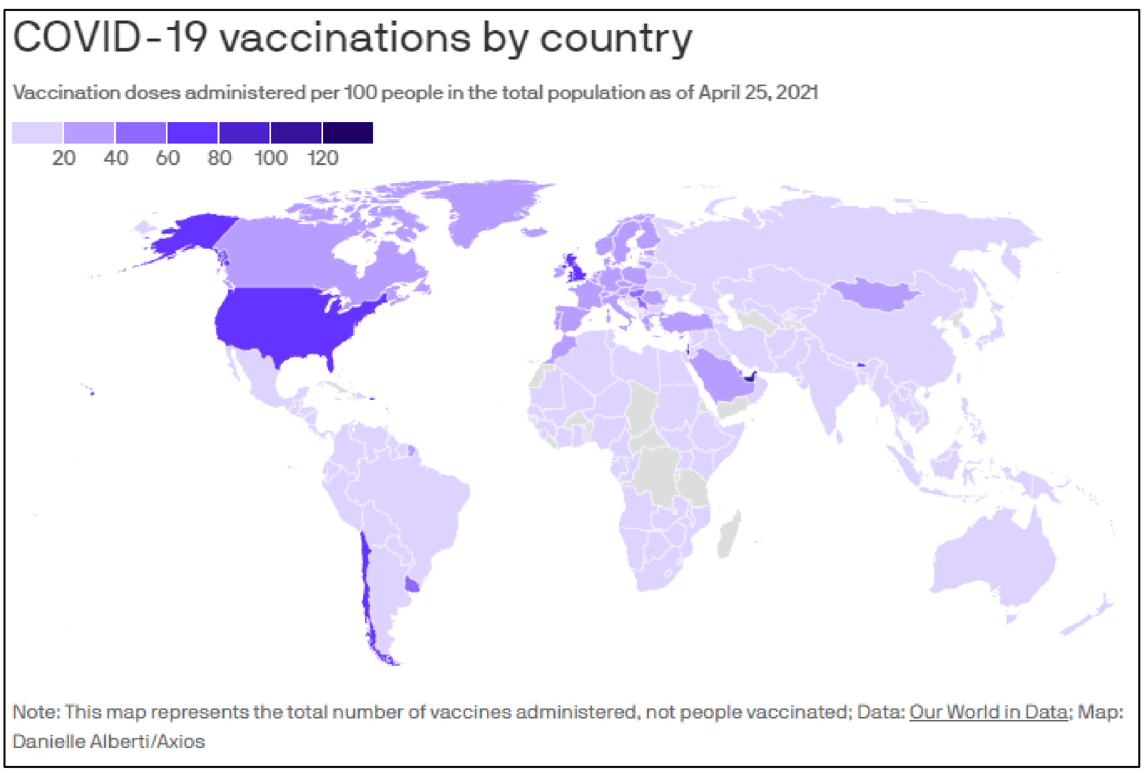
Chart 12. But isn't a yuge double deficit poison for a currency?

Source: Macrobond and Nordea

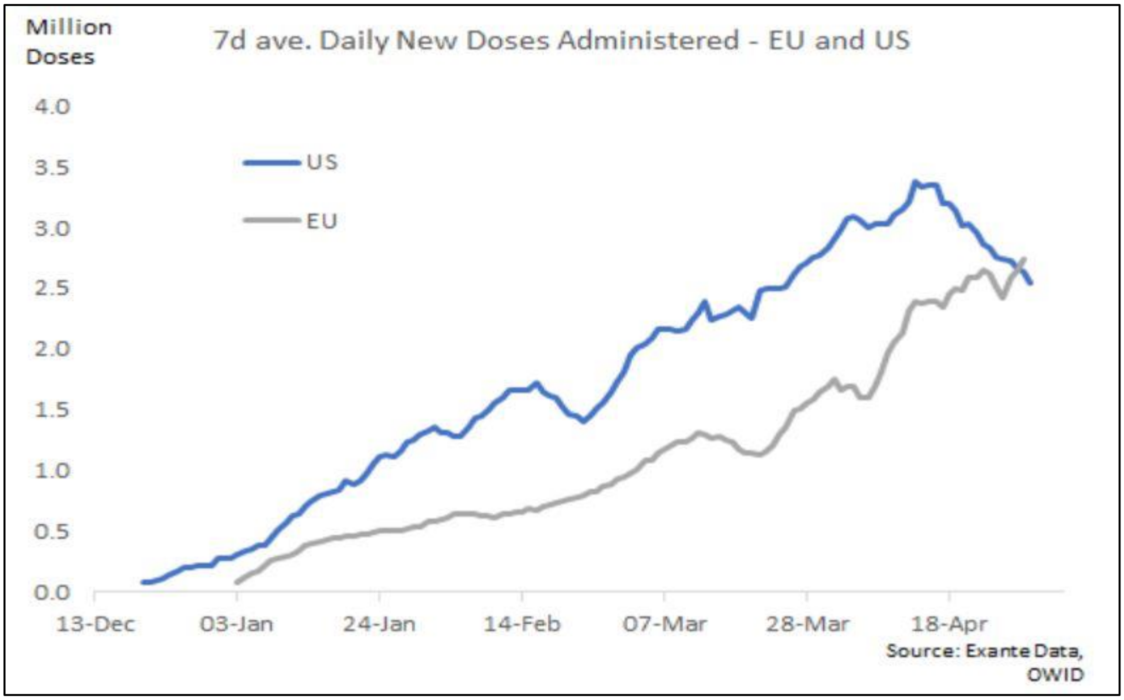
The bull case…



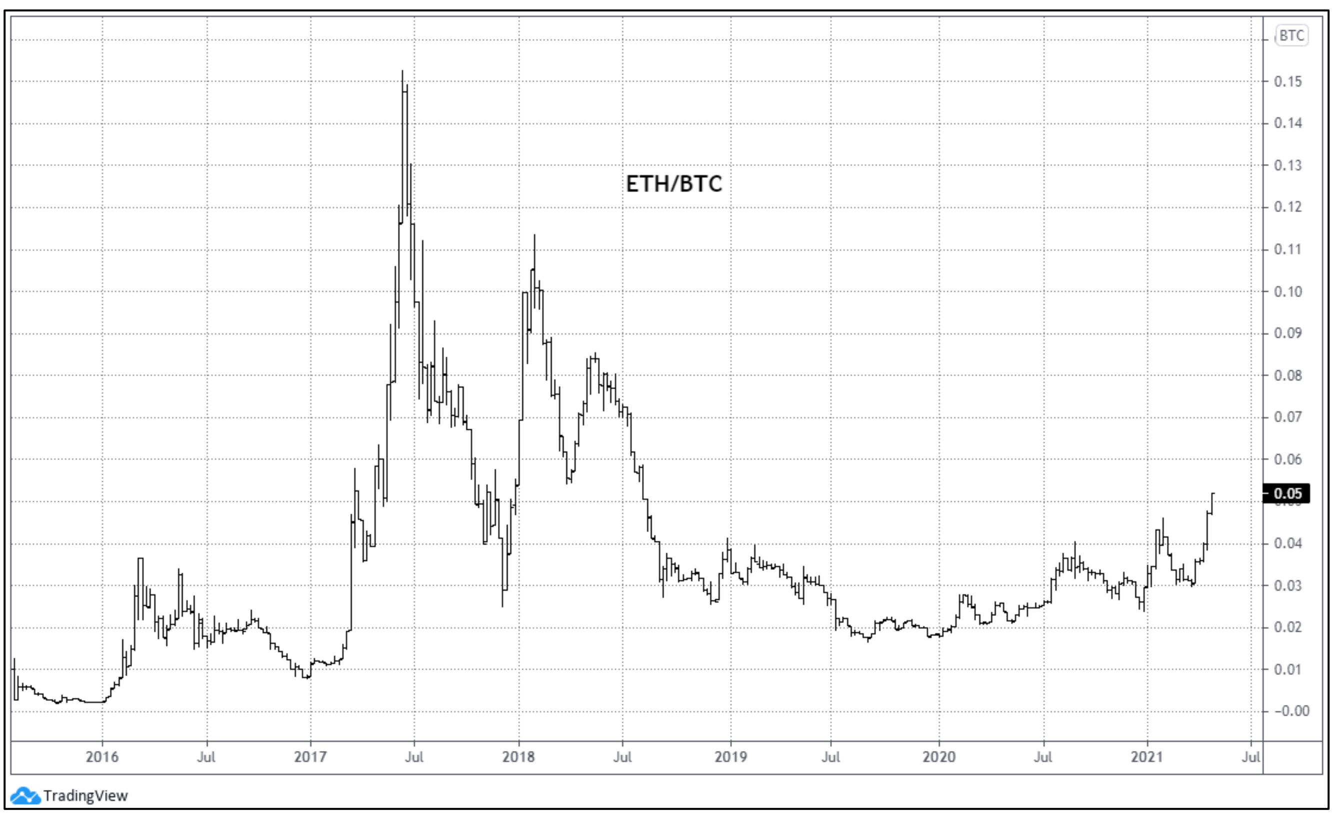
The much better vaccine rollout…



Finally, some other DM countries are coming online, EM is still way behind however.



Crypto chart of the week – Ethereum is starting to outperform Bitcoin. Relative breakout?



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Next week we have US jobs data and April PMI's from around the world. The employment numbers are going to be very important going forward as they will have a big impact on when tapering of asset purchases begins. March was +916k and Powell said they "want to see a string of months" like that. The unemployment rate should break back below 6%.

Also, we have monetary policy decisions from the BoE and the RBA.

Important Macro Data Releases and Events for the Week

Monday 5/3/2021

- Retail Sales YoY (Mar) Forecast: -3.1%, Prior: -9%
- Markit Manufacturing PMI's across Europe
- Markit Manufacturing PMI (Apr) Forecast: 60.6, Prior: 60.6
- ISM Manufacturing PMI (Apr) Forecast: 65, Prior: 64.7
- ISM Manufacturing Employment Index (Apr) Forecast: -, Prior: 59.6
- ISM Manufacturing Prices Paid (Apr) Forecast: 85, Prior: 85.6
- ISM Manufacturing New Orders Index (Apr) Forecast-, Prior: 68
- Fed's Williams SPEECH
- **Fed's Chair Powell SPEECH**

Tuesday 5/4/2021

- RBA Interest Rate Decision and Policy Statement
- Trade Balance (Mar) Forecast: $-74bln, Prior: $-71.1bln
- Factory Orders MoM (Mar) Forecast: 1.1%, Prior: -0.8%

Wednesday 5/5/2021

- Markit Service PMI's across Europe
- ADP Employment Change (Apr) Forecast: 808k, Prior: 517k

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- Markit Services PMI Forecast (Apr): 63.1, Prior: 63.1
- Markit PMI Composite (Apr) Forecast: 62.2, Prior: 62.2
- ISM Services New Orders Index (Apr) Forecast: 56.6, Prior: 67.2
- ISM Services PMI (Apr) Forecast: 64.3, Prior: 63.7
- ISM Services Employment Index (Apr) Forecast: 55, Prior: 57.2
- ISM Service, Prices Paid (Apr) Forecast: 73.3, Prior: 74
- BoJ Monetary Policy Meeting Minutes
- Caixin Service PMI (Apr) Forecast: -, Prior: 54.3

Thursday
5/6/2021

- Factory Orders s.a. MoM (Mar) Forecast: 1.9%, Prior: 1.2%
- Economic Bulletin
- Retail Sales YoY (Mar) Forecast: 9.4%, Prior: -2.9%
- BoE Interest Rate Decision and Monetary Policy Report
- Fed's Williams SPEECH
- Initial Jobless Claims Forecast: 540, Prior: 553k
- Initial Jobless Claims 4-week average Forecast: -, Prior: 611.75k
- Continuing Jobless Claims -, Prior: 3.66
- Unit Labor Costs (Q1) Forecast: -0.7%, Prior: 6%
- Nonfarm Productivity Q! Forecast: 3.5%, Prior: -4.2%
- RBA Monetary Policy Statement
- Trade Data

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Friday
5/7/2021

- Trade Data
- **Nonfarm Payrolls (Apr) Forecast: 950k, Prior: 916k**
- **Average Hourly Earnings (Apr) Forecast: 0.1%, Prior: -0.1%**
- **Average Hourly Earnings YoY (Apr) Forecast: -0.3%, Prior: 4.2%%**
- **Labor Force Participation Rate (Apr) Forecast: -, Prior: 61.5%**
- **Unemployment Rate (Apr) Forecast: 5.7%, Prior: 6%**
- Unemployment Rate and Net Change (Apr)
- Ivey PMI s.a. (Apr) Forecast: 60.5, Prior: 72.9

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