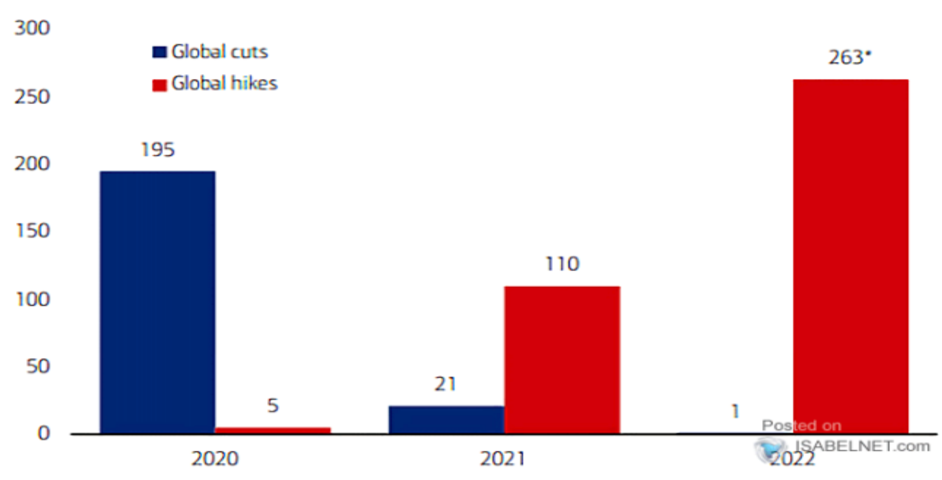
Stargazer
Asset Management

What to focus on in Global Macro for the week of April 18th, 2022

Global central banks have now swung aggressively from broad-based easing at the start of the pandemic in 2020, to widespread tightening on high inflation driven by goosed demand and persistent supply constraints.

Chart 8: Central banks on course for biggest tightening this century
Global rate cuts vs hikes



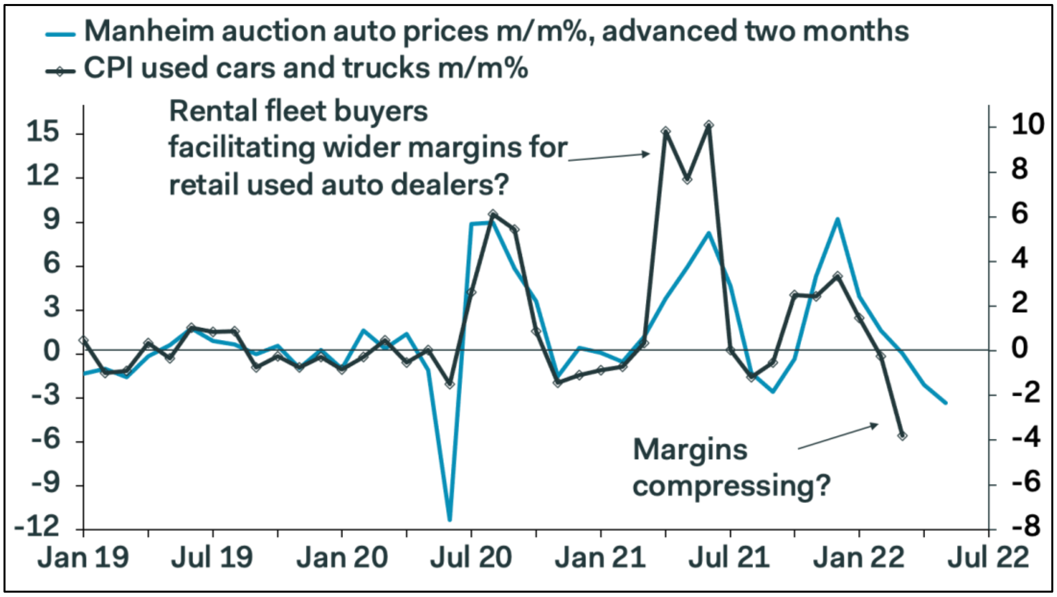
Source: BofA Global Investment Strategy, Bloomberg
Note: 2022 annualized

Going forward, it will be interesting to see how growing policy divergences between major economic blocks evolve. The US and other selected countries have embarked on an aggressive tightening cycle, while Europe is less convicted, facing a deteriorating growth environment and high inflation. At the same time, Japan is resisting the global interest rate rises and China's COVID policies are dramatically slowing their economy, forcing reluctant policymakers to loosen monetary conditions.

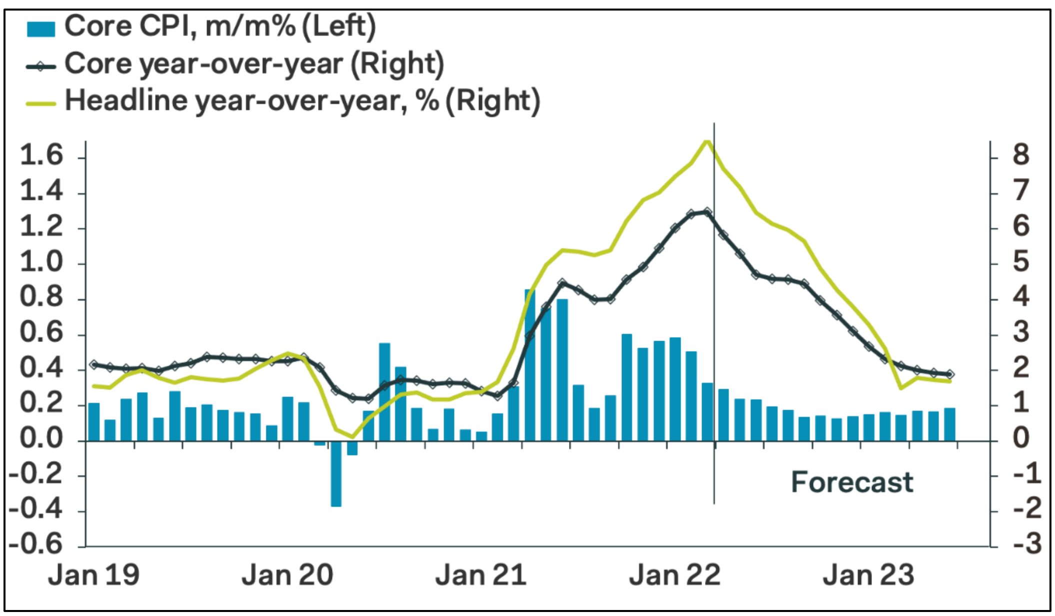
Last week's ECB meeting confirmed plans to roll back stimulus but also warned that it was very contingent on how the growth conditions developed. Most of the inflation in Europe has been driven by energy prices which also act as a tax on consumption, leaving growth vulnerable. With quite a few hikes priced there is a lot of room for volatility in European rates markets over the next few months, and in the EUR.

US CPI and PPI came in high. PPI was particularly ugly as it tends to foreshadow CPI, but divergences can happen in this unusual situation.

CPI was high as expected but some initial signs of a turn are emerging. Used car prices are coming off the boil. The May hike looks almost certain to be 50bps, but a further softening of car prices could reduce the likelihood of another 50bps in June.



Most economists still see base effects kicking in starting with the next couple of data prints. How far and how fast inflation falls will be key, however.



China - Last week, the PBoC begrudgingly cut the RRR. We will see if they cut rates next week.

As Pantheon Macro wrote:

"A 25bp cut, assuming no further action this month, is the smallest monthly change in the RRR on record. Even with this RRR cut, the PBoC has still withdrawn liquidity on a net basis so far this month, thanks to repo operations, as our chart below shows. The central bank continues to argue

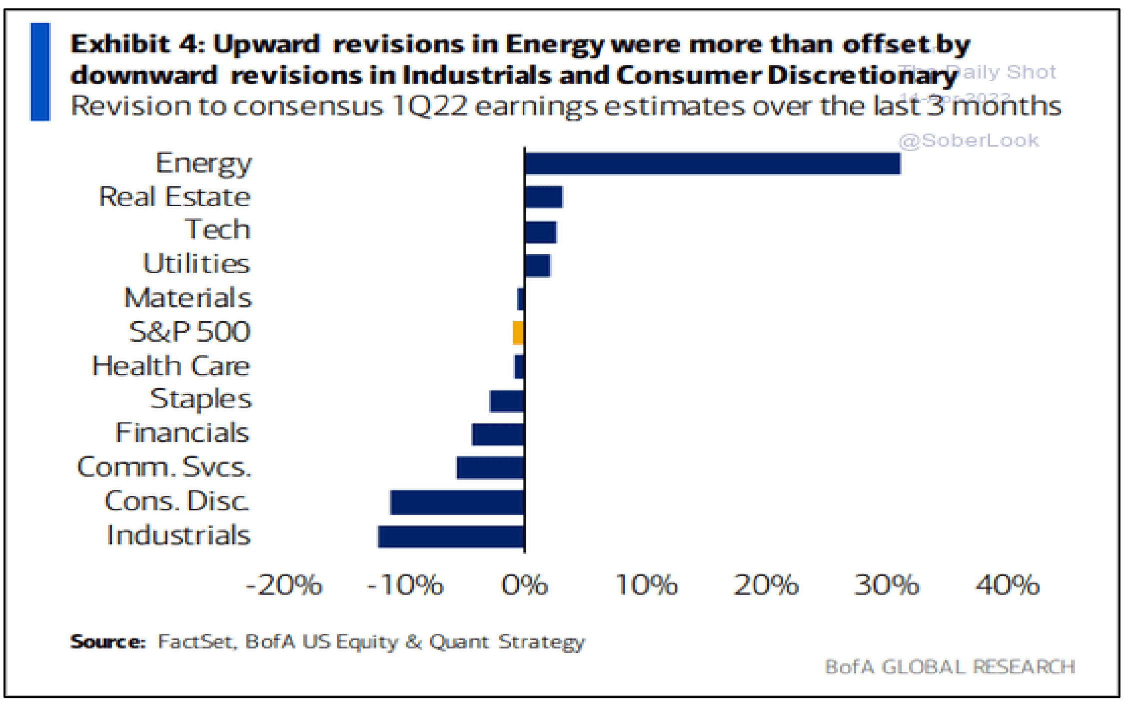
that monetary transmission, not policy, is the main problem, and urged banks to cut deposit rates today, to aid the recovery.

The real problem is the weakness of the economy. Zero-Covid, and the property downturn, alongside growing export headwinds, are sapping confidence and activity. Demand for loans remains weak, as the PBoC's Q1 survey showed, because the prospects of making a decent return on a commercial investment are low, and no one in their right mind will buy a house from a developer which may go out of business before finishing construction. Banks, unsurprisingly, are unwilling to lend to the kind of borrowers who still want credit in this environment, because the likelihood of repayment is much lower. Rate cuts will therefore have minimal effect on economic growth, without a jolt to demand. Fiscal stimulus, however, still looks focused on supply side issues."

Markets

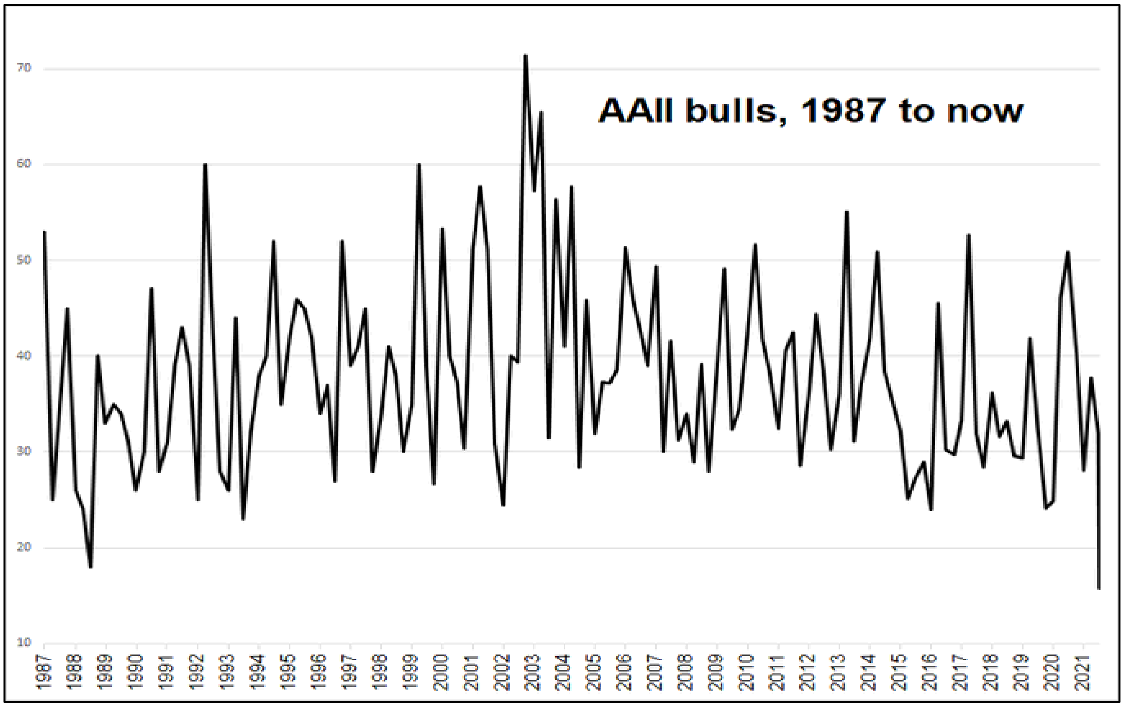
Equities closed poorly for the week but still find themselves near the middle of the range for the last three months.

The flailing indices hide some of the extreme divergences we are seeing between the sectors.

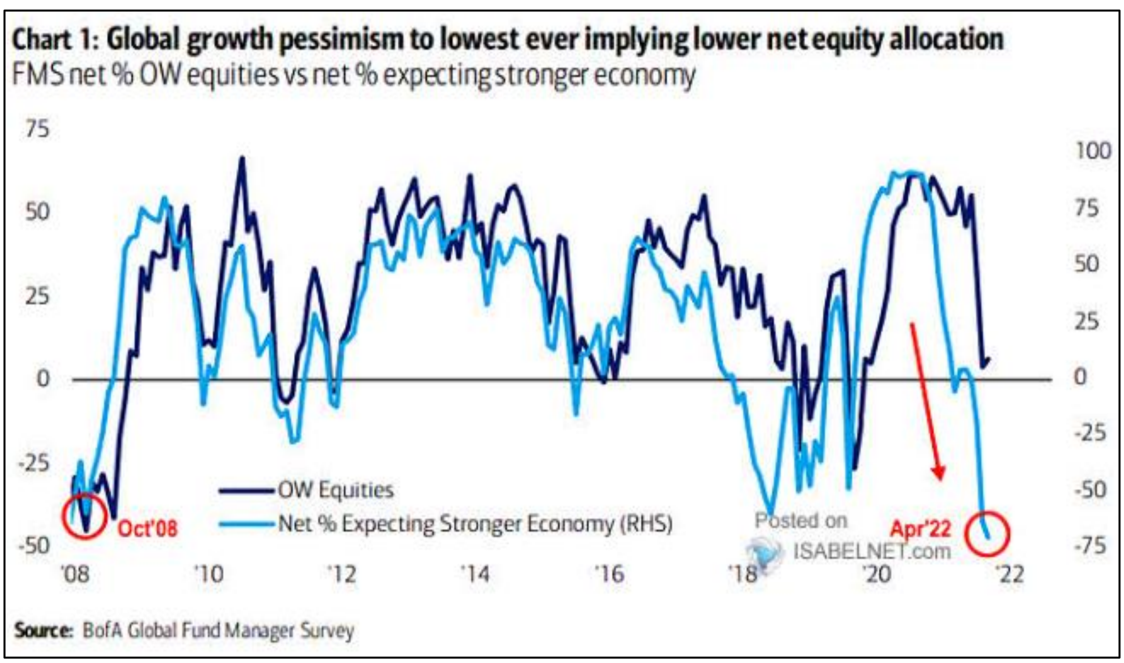


At the same time, despite the indices holding up well in aggregate given the Macro setup, sentiment for equities overall and for global growth has become very pessimistic.

It remains to be seen if the bearishness proves to be prescient or a contrarian fade.



So far, the narratives of TINA, buyback announcements, "stocks do well when the Fed hikes", "stocks look through geopolitics", and easing inflation will allow the Fed to pull off a soft-landing.



More interesting than the indices at the moment, are some of the sector paired trades.

Real Estate continues to lurk just below resistance vs. the S&P.

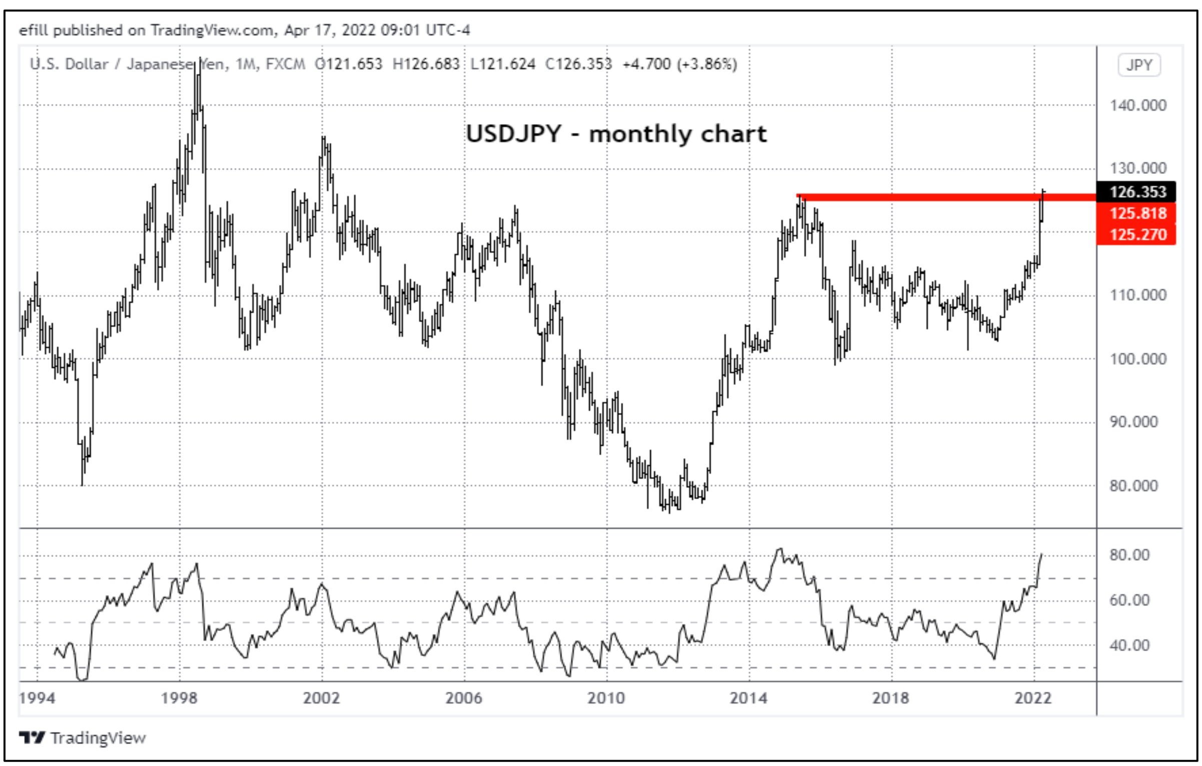
Given the desire for materials and the worry about long-duration assets, it is no wonder that XLK/XLB has been under pressure. This looks like it has more downside. Keep in mind these are weekly charts, so need some wiggle room.

Continuing with that theme, Metals and Mining have arguably seen a long-term break higher.

As have global natural resource stocks. Although ideally, they need to hold above the trendline.

The longer-term outlook for agribusiness is looking more promising as well, vs. the broader market. Tight grain and fertilizer markets are pushing it.

FX – We are at big levels for the dollar vs. the negative yielders, as the US leads the cycle.



With an uncertain outlook in Europe, EURUSD has been toying with the 1.0800 level.

The USD has even been bumping up against the top of its range vs. CHF

Wheeling out a continuous Deutsche Mark chart (including extrapolation from the EUR since '99) illustrates the importance of the current levels.

<u>Over the last few decades, every financial crisis has been accompanied by a strengthening USD.</u> As the global reserve currency, there is a global liquidity effect here, and the cause/effect seems to exhibit strong reflexivity during these periods. Is it different this time?

Currently, there is a lot of dispersion among currencies, as commodity producers have been doing relatively well, while low-yielding DM countries have done poorly vs. USD. The DXY is heavily affected by its 57% allocation to the EUR and 13% allocation to JPY, so arguably it is only reflective of a part of the story. Still, as economic blocks go, Europe and Japan are sizable parts of global GDP, and as such, can't easily be discounted.

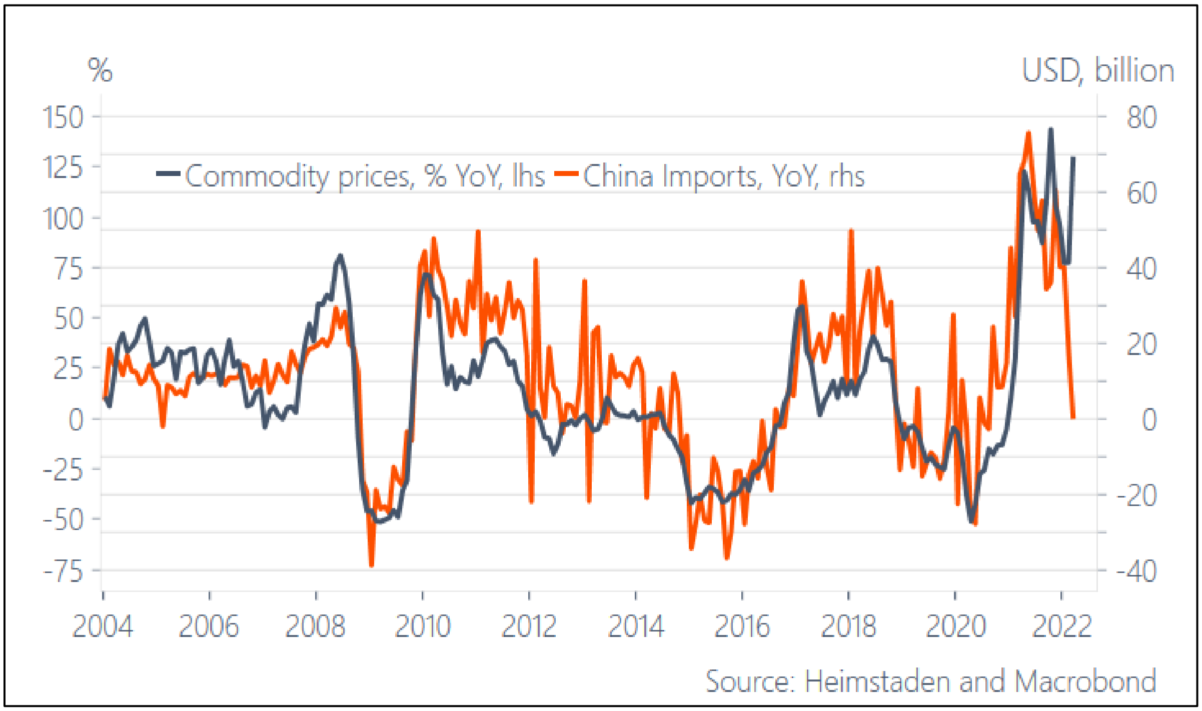
As discussed earlier, China has started to ease up further on its monetary policy stance. So far, its balance of trade advantage has kept the currency stronger than you might imagine in the current environment.

We will see if easier monetary policy and growing growth challenges from internal policy and COVID lockdowns will now challenge the currency.

China / US 10-year spreads are now again negative…

Watch for a close above 6.3950 in USDCNH.

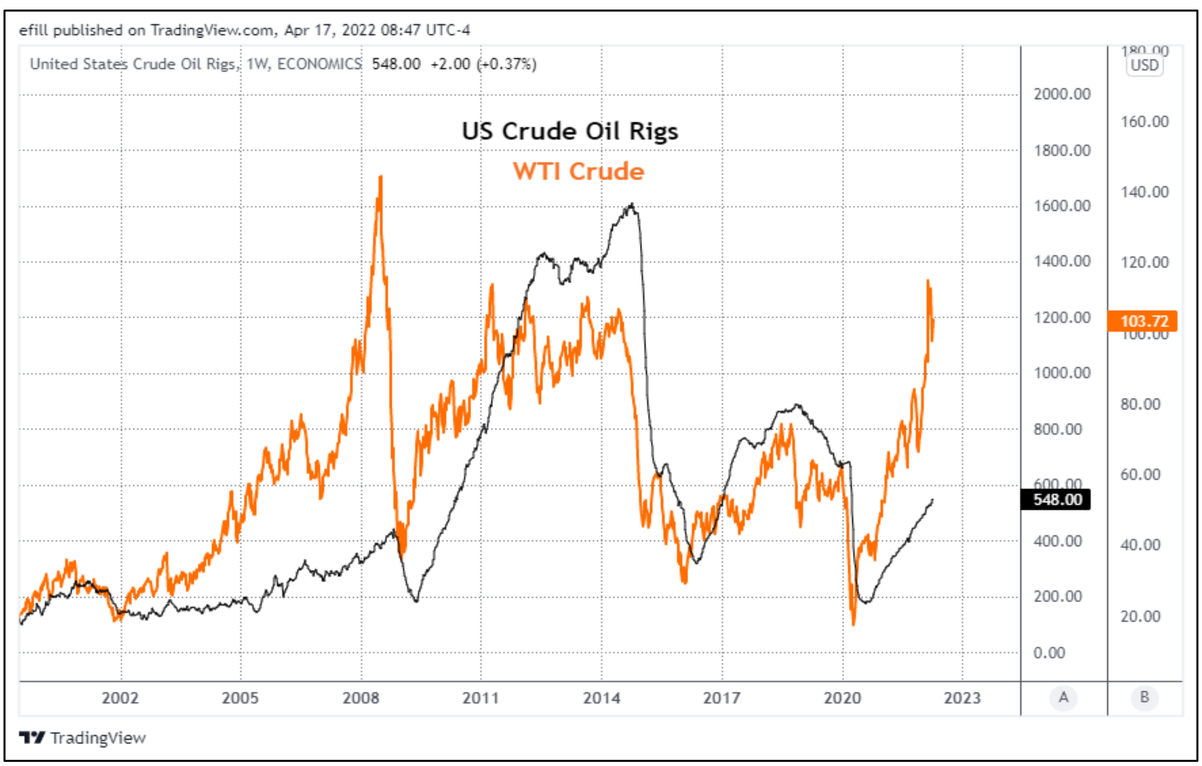
In a pre-COVID world slowing Chinese import demand would be a warning sign for global commodity prices. However, with supply constraints still overpowering marginal demand shifts we will see if it matters…



In the meantime, near-term energy supplies and prices remain the focus. US Nat Gas…

The backwardation in Oil futures still speaks to the view that a good deal of the price spike is temporary. Here front oil vs Dec. 2025

With the industry disincentivized to make capital expenditures the rig count is slow to respond.



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In the meanwhile, economic "Dr. Copper" is about where it was a year ago. Inventories and production capacity remains low, but lower Chinese demand is balancing that for now.

Gold has been trying to achieve escape velocity. I had been looking for a close above 1960, which has been achieved. Next up, 1980...

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Important Macro Data Releases and Events for the Week

Monday 4/18/2022	Sunday Night ET - GDP, Industrial Production, and Retail Sales (think lockdowns)
	Fed's Bullard speech
	IMF Meetings all week
	RBA Minutes
Tuesday 4/19/2022	Fed's Evans speech
	SNB's Chairman Jordan's speech
	PBoC Interest Rate Decision
Wednesday 4/20/2022	CPI (Mar)
	Fed's Beige Book
Thursday 4/21/2022	Philly Fed Manufacturing Survey (Apr)
	Initial Jobless Claims
	Initial Jobless Claims 4-week average
	Continuing Jobless Claims
	Fed's Chair Powell speech
	BoE Governor Bailey speech
Friday 4/22/2022	Flash PMIs across Europe and US (Apr)
	BoE's Governor Bailey speech

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