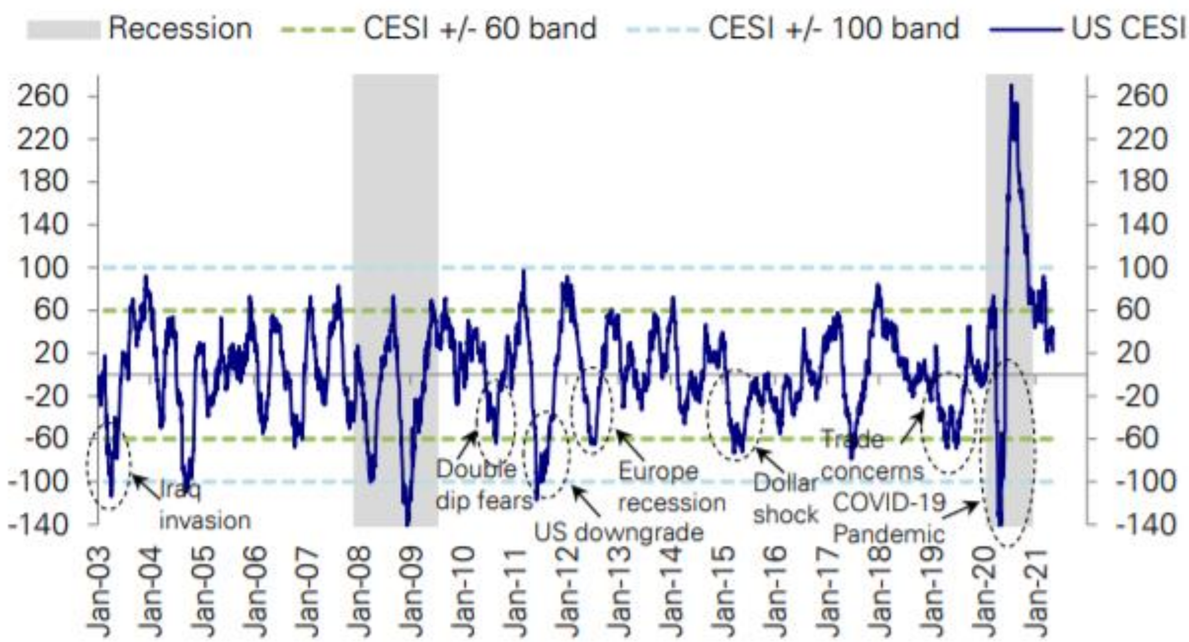
What to focus on in Global Macro for the week of May 10th, 2021

Macro Themes on the Radar:

Over the last few weeks, investors have increasingly switched their attention from epidemiology back to economics. However, now that the previous run of positive data surprises has returned to a more normal mix of data beats and misses, investors are finding it harder to see the forest for the trees.

Figure 9: Data surprises have returned to their normal range after a prolonged period at unprecedented highs



Source : Citigroup Economic Surprises, Haver, Deutsche Bank Asset Allocation

The unprecedented nature of COVID's effects on the economy and the resulting global government response has people very confused about what comes next. The economy first hitting the breaks then hitting the gas has everything shaken up. Bottlenecks in supply and demand are the name of the game in both employment and manufacturing.

Of course, last week's miss on the US jobs data is a great example. Not only does it highlight the economic uncertainty, but it also brings the fiscal and monetary policy debate front and center.

Some Fed members were quick to point out how the number vindicates their new outcomes vs. expectations framework.

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"For all those people who have been saying 'oh my gosh, the Fed needs to normalize quantitative easing,' today's job report is just an example of – we have a long way to go," the Fed's outspokenly dovish Neel Kashkari said, in an interview on Bloomberg Television.

Reasons cited by analysts for the weaker than expected numbers include:

- Enhanced UI benefits are keeping people from returning to work.
- Schools and day-cares haven't fully reopened, and this is keeping many mothers from returning to the labor force.
- Supply-chain bottlenecks are constraining production in some key industries.
- The government's "seasonal adjustment" formula is at least partially to blame.
- It takes time for a labor market to recover from a pandemic.

How the reasons for the miss are portrayed, has quickly come down along political lines. Right-leaning commentators blame the enhanced benefits. According to the WSJ, "A University of Chicago study found 42% of those on benefits receive more than they did at their prior jobs, and the share is higher when factoring in temporary health insurance offered through relief bills."

While those leaning left are pointing to day-care and lasting economic damage as the cause. Senior economist at the left-leaning Economic Policy Institute, Heidi Shierholz, said unemployment benefits' disincentive effect is overstated and that the pandemic caused a huge disruption in the labor market and it will take time for the dust to settle. She added that "if the extended benefits mean some workers can take the time to find a job that's a better match for their skills and pays them a better wage, that's a good thing, not a bad thing".

Anecdotal evidence, as well as the actual breakdown of the numbers, seems to indicate that all these forces appear to be contributing factors. The US Commerce Department is calling for the removal of the supplemental benefits and at least one Republican Congressman is introducing a Bill to end the payment before they are set to run out in September.

What the employment number does do, is pour some cold water on the growing calls for an early start to tapering. The counter for Powell's "string" of good employment numbers that would trigger the taper debate, seems to now have been reset to zero.

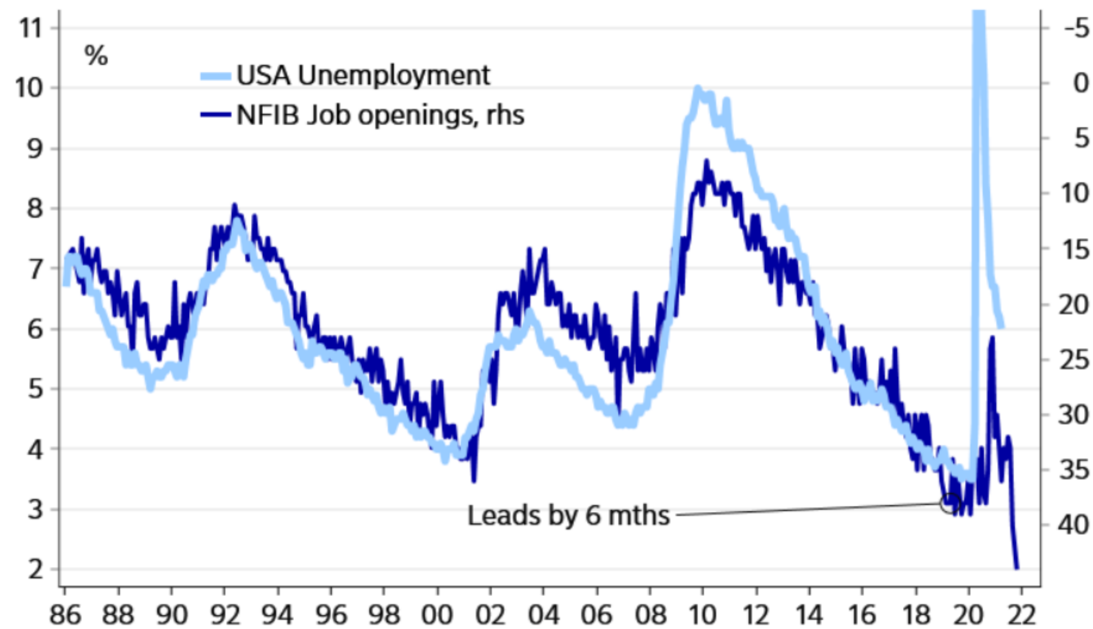
The May employment data will look large as investors will look for confirmation that something is holding back progress or that the blockage is clearing.

Now add the increasingly furious debate on whether the expected coming inflation spike will be temporary or more lasting, and we have growing uncertainty on a number of fronts.

There is still plenty of potential for both employment and inflation to jump dramatically in the coming months. I still wonder if both surprise with their strength.

How big these jumps are vs. the expectations of increasingly confused investors could make for some messy price action across markets.

Chart 4. Record-high share of small US companies with job openings



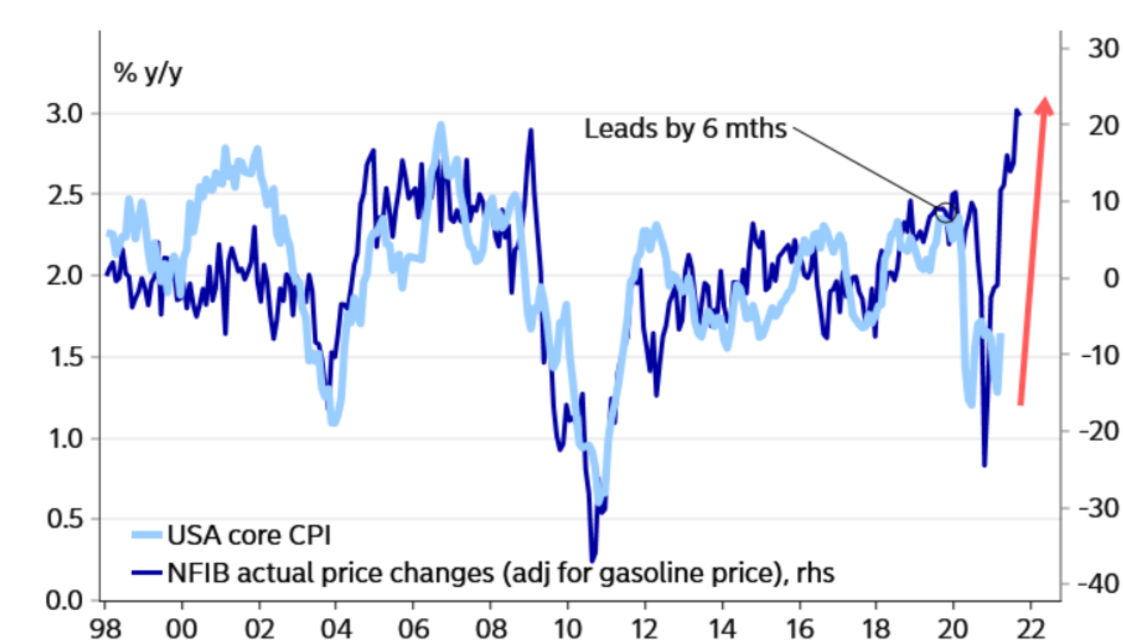
Source: Nordea Markets and Macrobond

Chart 5. Supply/demand/inventory strains usually take time to sort out

Source: Macrobond and Nordea

The united front of resolute dovishness that we have seen from the Fed over the last few months is starting to crack a bit as the coming jump in inflation is discounted. The Fed's Rosengren said last week that inflation reaching a number not starting with 2 would worry him.

Chart 12. US small businesses are hiking prices en masse



Source: Macrobond and Nordea

Last week we saw some weakness in ISM numbers. Eventually, of course, these high levels will be unsustainable, but that probably requires a multi-month topping process.

Interestingly, this initial downtick may not be what it seems. It seems that rather than a lack of demand, but rather bottlenecks in both the availability of inputs and labor is behind it. More fuel on the fire for now.

For the moment, the Fed must feel that the pressure to taper is off, but some economists like El-Erian, were quick to point out that this is not the case. Continued further easing of financial conditions, via $120bln a month of QE, will be increasingly difficult to justify. However, it does give them some breathing room and makes tapering before the end of the year unlikely.

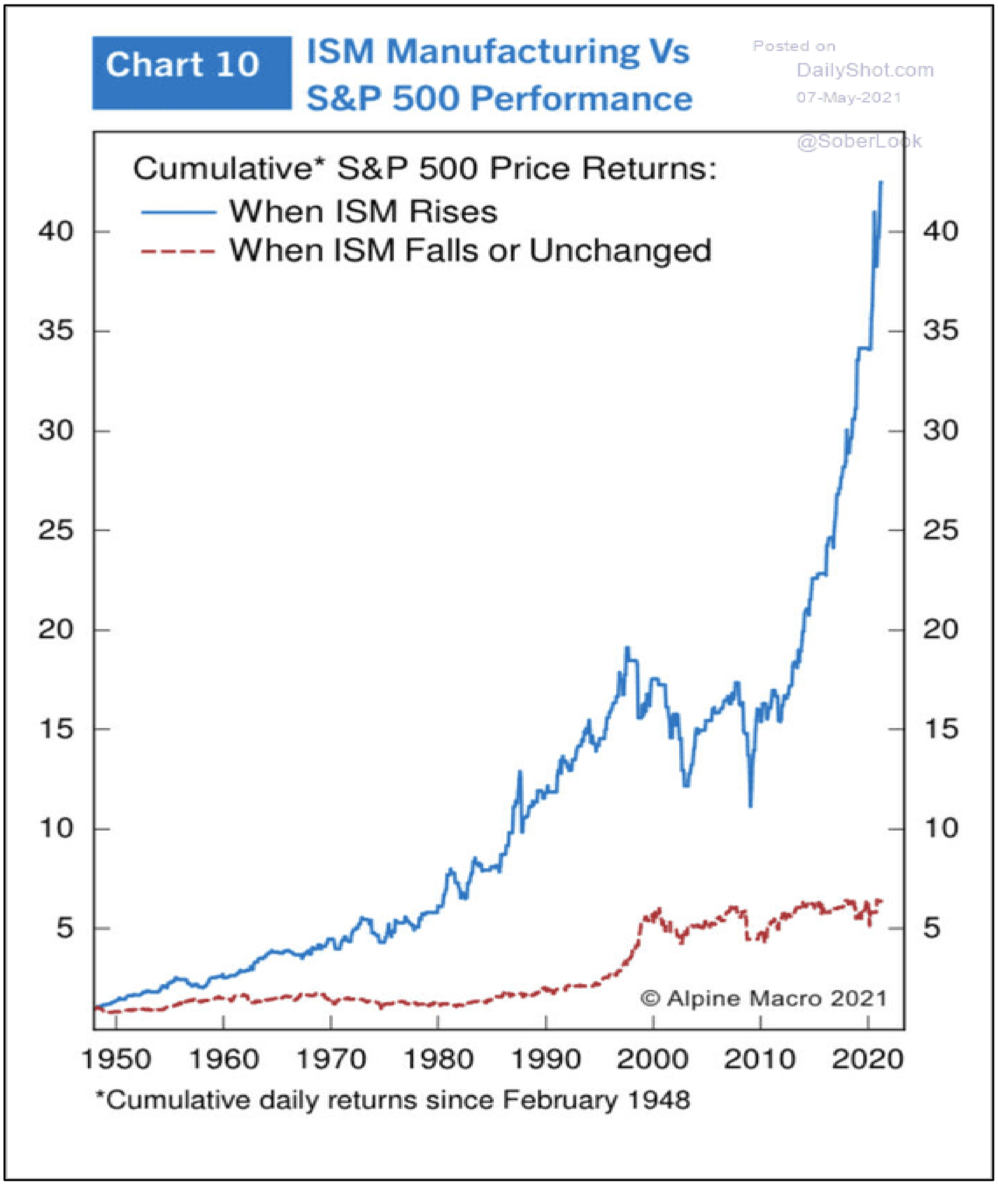
Given the meeting schedule and the “string” of good data requirements, a September announcement of a December taper looks feasible. The next few months of inflation and employment data prints with be show stopping events.

- June 2021 FED meeting date 15 – 16 June FOMC meeting
- July 2021 FED meeting date 27 – 28 July FOMC meeting
- September 2021 FED meeting date 21 – 22 September FOMC meeting
- November 2021 FED meeting date 2 – 3 November FOMC meeting
- December 2021 FED meeting date 14 – 15 December FOMC meeting

What to Focus on Now:

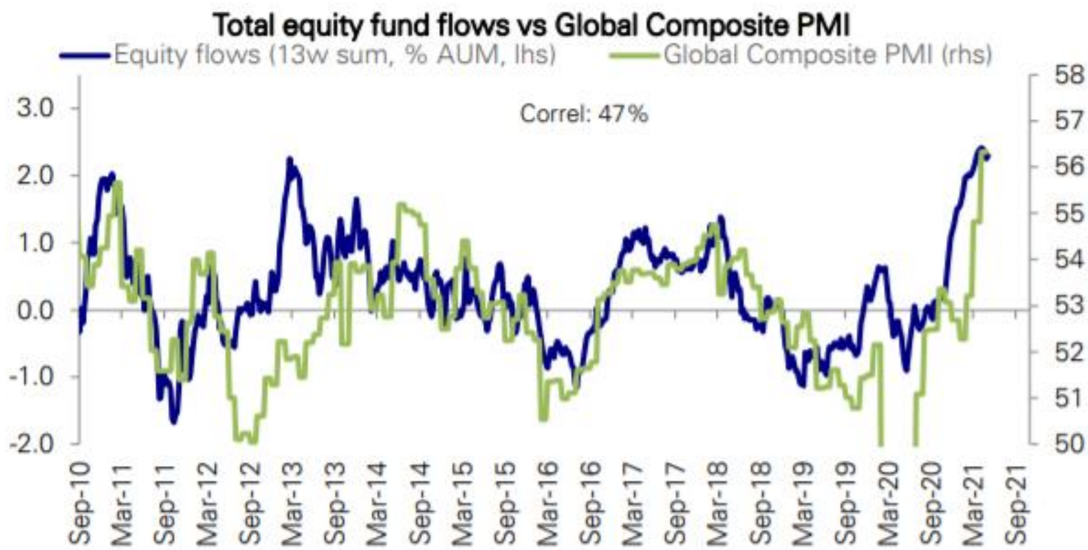
Equities

Equities have remained strong as capital has continued to flow into the asset class. Stocks have continued to be supported by expectations. Rising ISM and global PMI's are historically very correlated with the best performance periods for equities.



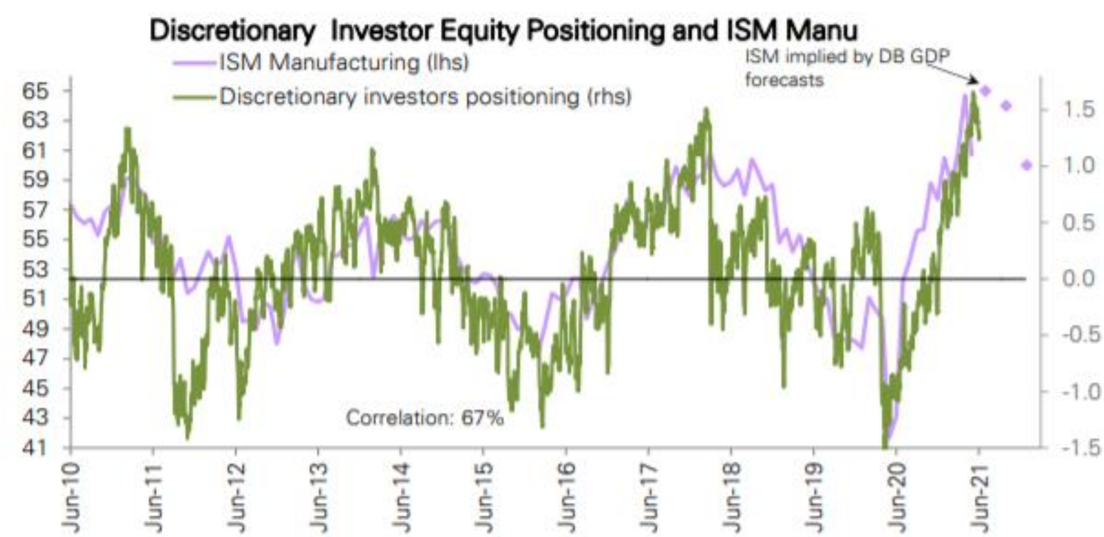
Equity flows and positioning have a strong relationship with those growth indicators as well.

Figure 6: Equity flows surged along with global growth and now look to be slowing



Source :EPFR, Markit, Haver, Deutsche Bank Asset Allocation

Figure 5: Discretionary positioning tends to be closely tied to indicators of growth

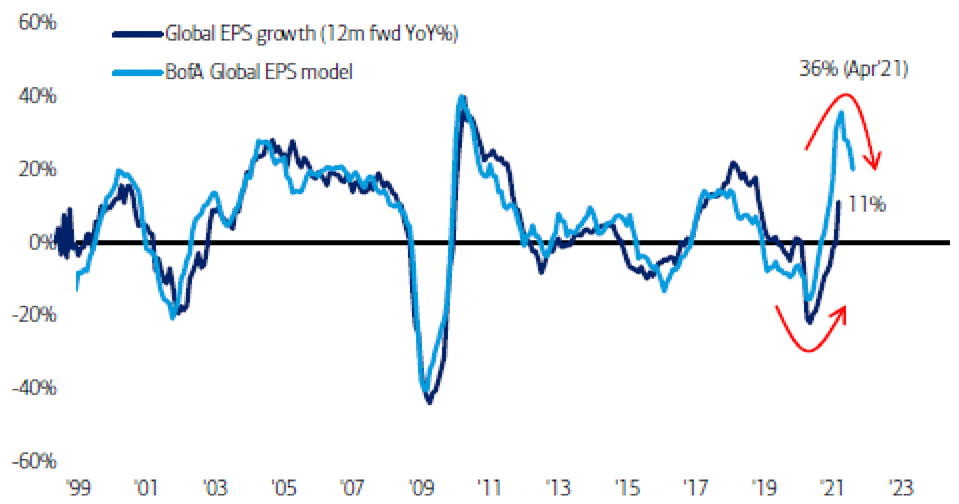


*Wtd avg Z-score across indicators; weights based on explanatory power in regression w/equity perf

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

Some earnings models are starting to call the top on EPS growth.

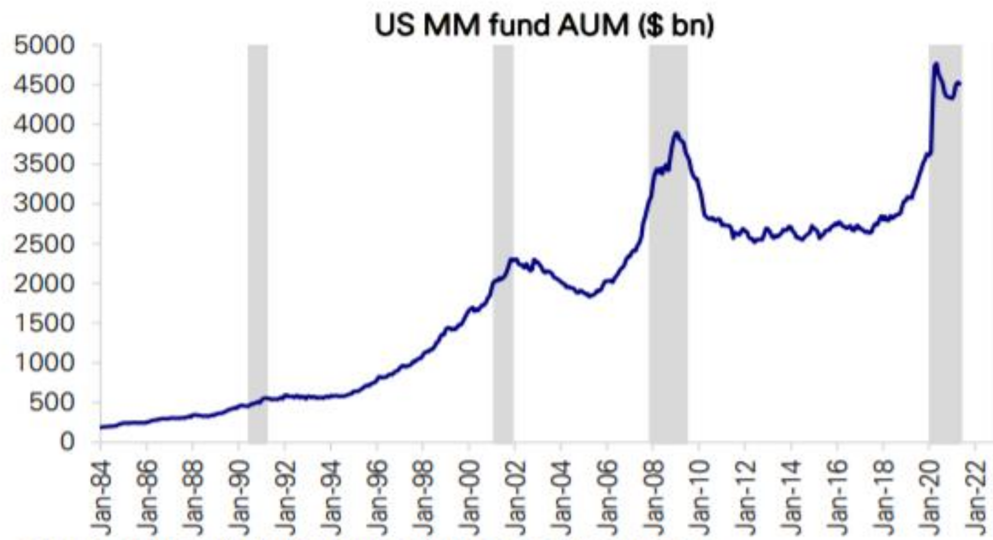
Chart 7: BofA Global EPS growth model says peak ≈ 36% in April
BofA Global EPS growth model vs consensus EPS (12-month fwd YoY%)



Source: BofA Global Investment Strategy, Bloomberg, Haver, Datastream; model composed of Asian export growth, global PMI, US Treasury yield curve & Chinese
BofA GLOBAL RESEARCH

Lots of talk about all the money in money market funds that can still come into the market.

Figure 21: Cash held in money market funds rose sharply last year and is yet to decline



Last 1 month data for MM assets estimated using weekly data

Source : ICI, Haver, Deutsche Bank Asset Allocation

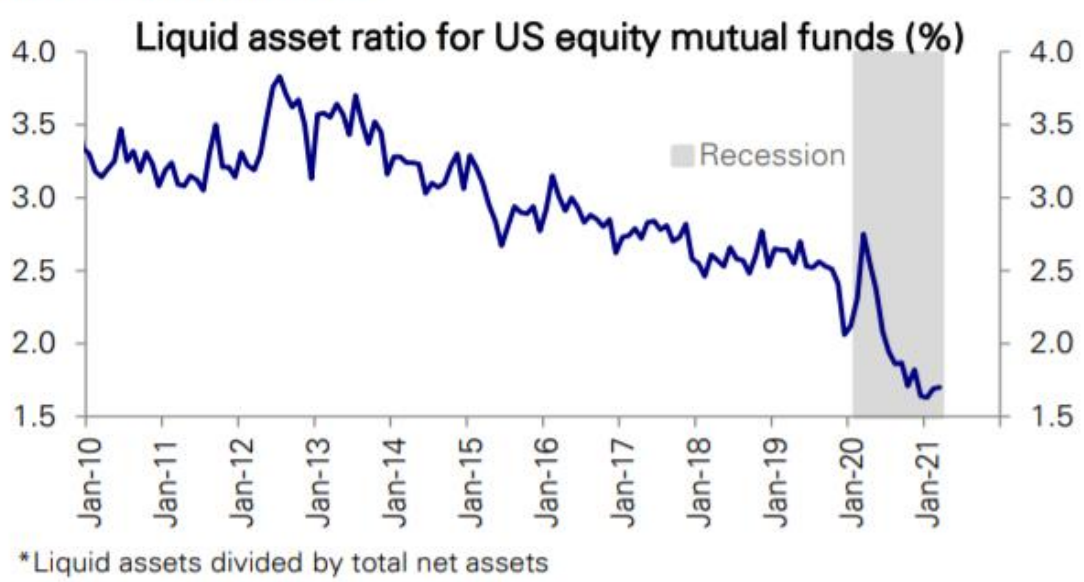
However, by some measures that could be overstated. Seen relative to market cap, for example.

Figure 23: However, as a proportion of equity market cap, MM fund assets are already near historical lows

Source : ICI, Haver, Deutsche Bank Asset Allocation

Cash held at mutual funds is already very low.

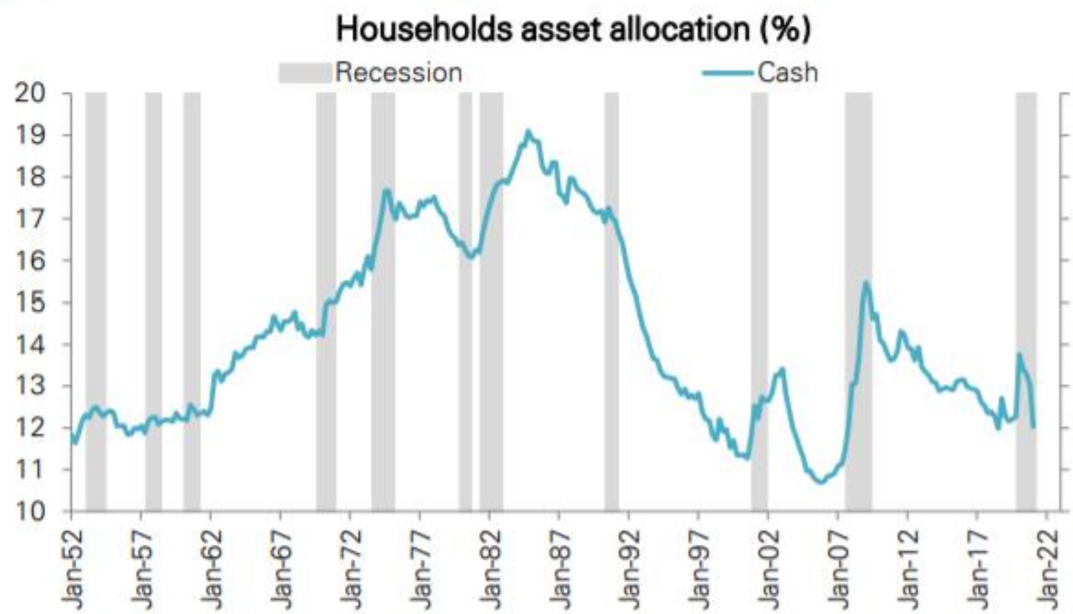
Figure 26: Cash held by equity mutual funds a proportion of their overall assets has also fallen to new lows



Source : ICI, Haver, Deutsche Bank Asset Allocation

Cash as a percent of total asset allocation is also at the low end of the range.

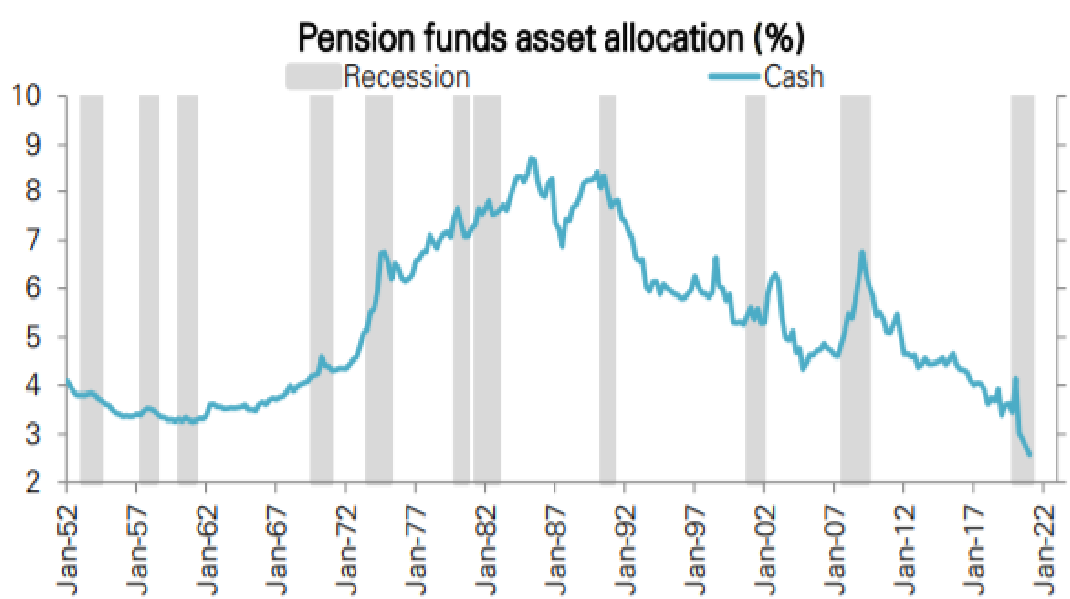
Figure 24: Allocations to cash by households are also very low



Source : FRB, Haver, Deutsche Bank Asset Allocation

As is cash at pension funds.

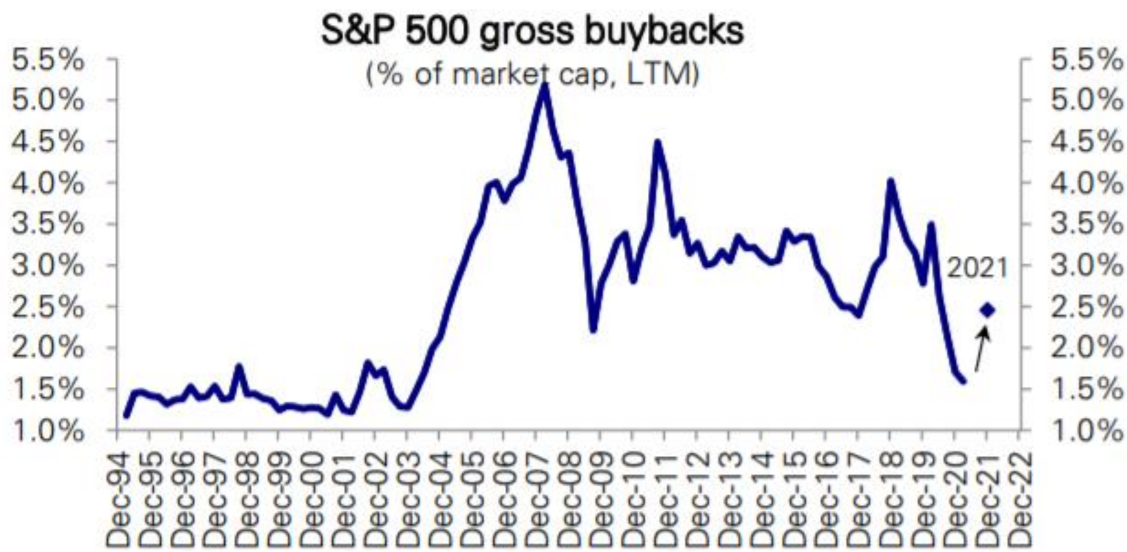
Figure 25: Pension funds allocation to cash has fallen to a new low



Source : FRB, Haver, Deutsche Bank Asset Allocation

Yes, buyback announcements have recently jumped substantially…

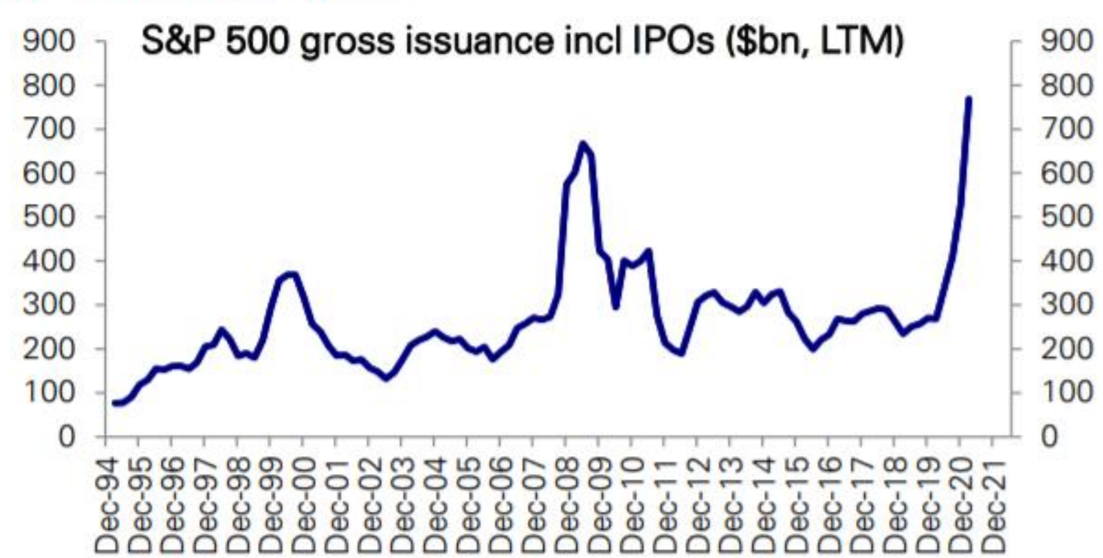
Figure 36: However, as a proportion of market cap buybacks are likely to rise only to the bottom of their pre-pandemic range



Source : Compustat, Bloomberg Finance LP, Deutsche Bank Asset Allocation

but in aggregate that could be offset by large issuance of new shares.

Figure 37: Meanwhile, if issuance continues to remain very strong it will largely offset even record buybacks



Source : Dealogic, Bloomberg Finance LP, Deutsche Bank Asset Allocation

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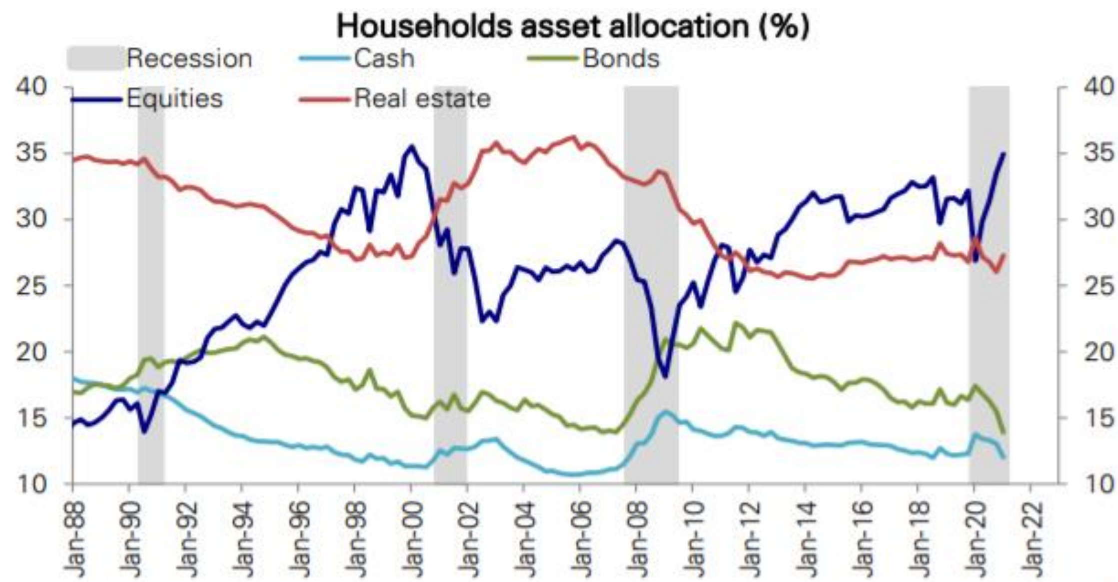
Allocation to equities is at, or near, record levels by most measurements, but of course, there is room for that to expand if investors continue to favor stocks over fixed income.

Figure 27: Household equity allocations are very high, those to other asset classes are very low



Source : FRB, Haver, Deutsche Bank Asset Allocation

US equities, while experiencing constant rotation, have held up very well in aggregate. The DJIA and SPX made new highs last week even as the NDX and Russell struggled. Signs of faltering momentum last week did not last. Europe, after a few weeks of post-breakout consolidation, was back near the highs by the end of last week as well.

Bonds - We saw one of the largest NFP downside misses of all time, and yet longer-term inflation breakevens didn't go down nor did bond yields when all was said and done.

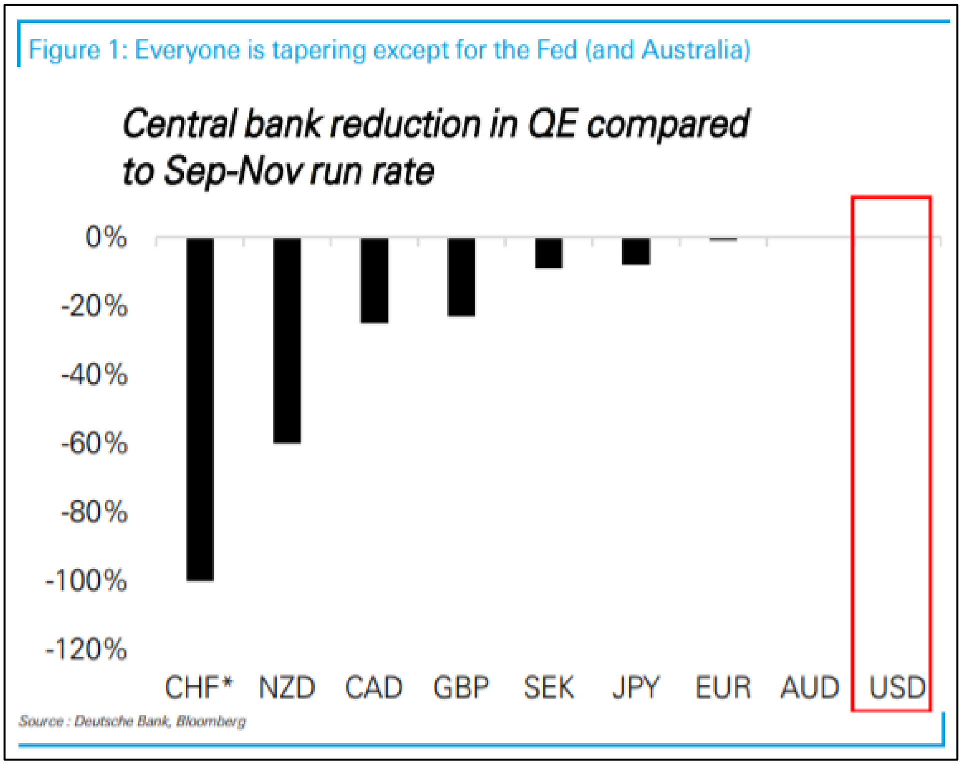
The bond market is looking through the weaker employment data and betting it will pass. In fact, no matter what you think the cause of the weaker data it is likely to do exactly that in the coming months. We should get some near-term calm given the Fed's "show me" approach, but then expect pressure to taper to start building again.

Back above 2.35 on the 30 year and you need to start paying attention again.

What could now again come back to life given the potentially delayed taper start, is dollar weakness.

FX

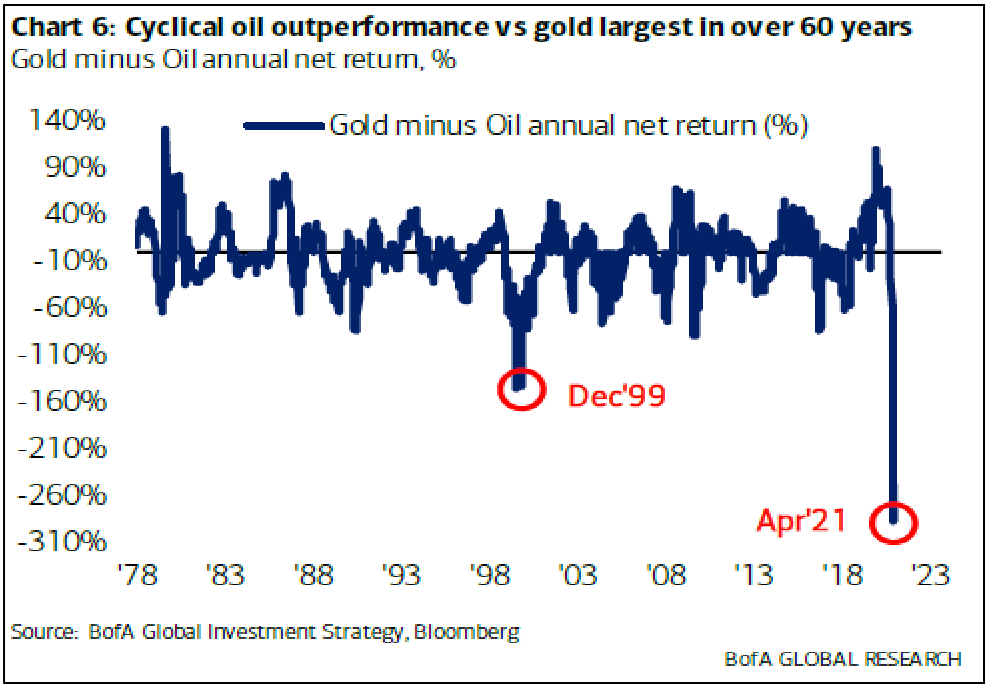
In theory, the weak employment data is a problem for the dollar. Not only does it extend the most dovish Fed stance, but it does nothing to imply a reduced current account deficit. In fact, potentially the opposite.



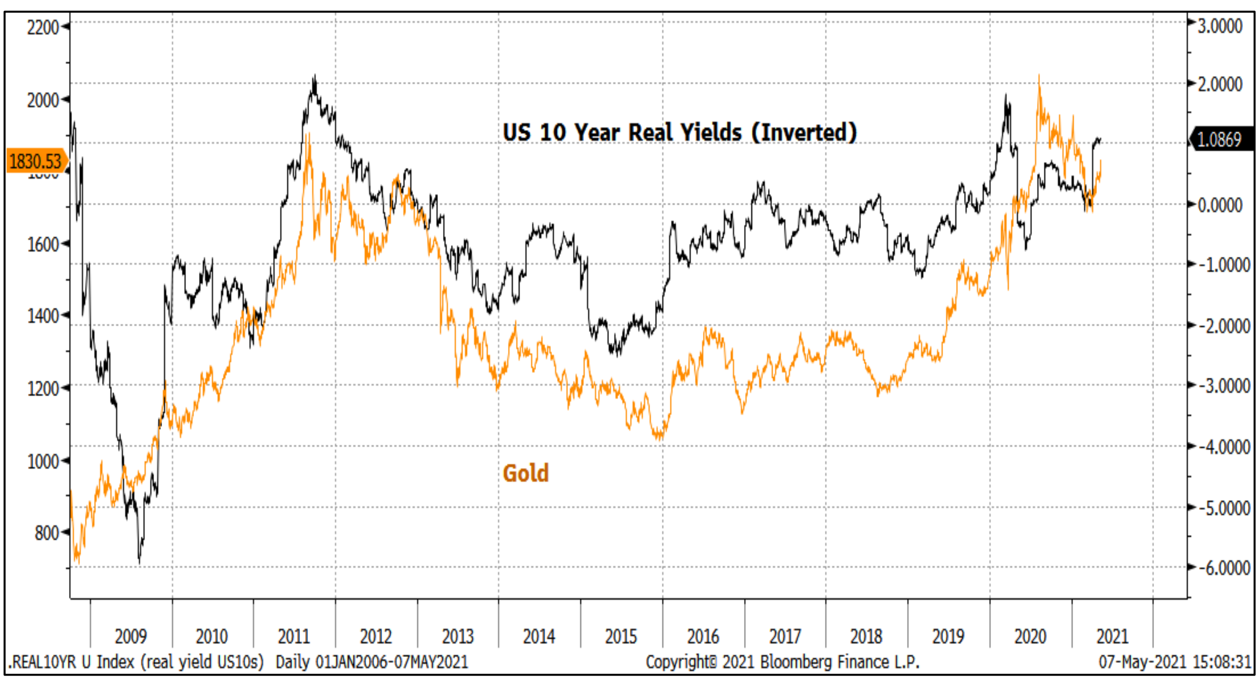
Multiple central banks have started to reduce QE. While we can debate whether all of the reductions in QE shown in the chart are really as labeled (like the UK), you get the point. No matter how you define it, the US has not eased off the gas pedal. That relative QE is potentially difficult for the dollar. We will know shortly if last week's break lower in the DXY is the start of a new leg lower for the dollar.

Gold & Silver

In the world of commodities, Gold and Silver have had a difficult time in recent months.



An initial rise in real yields, due to the jump in nominal bond yields, put downward pressure on the precious metals. Now real yields have again been falling and should fall further if we get the inflation pop.

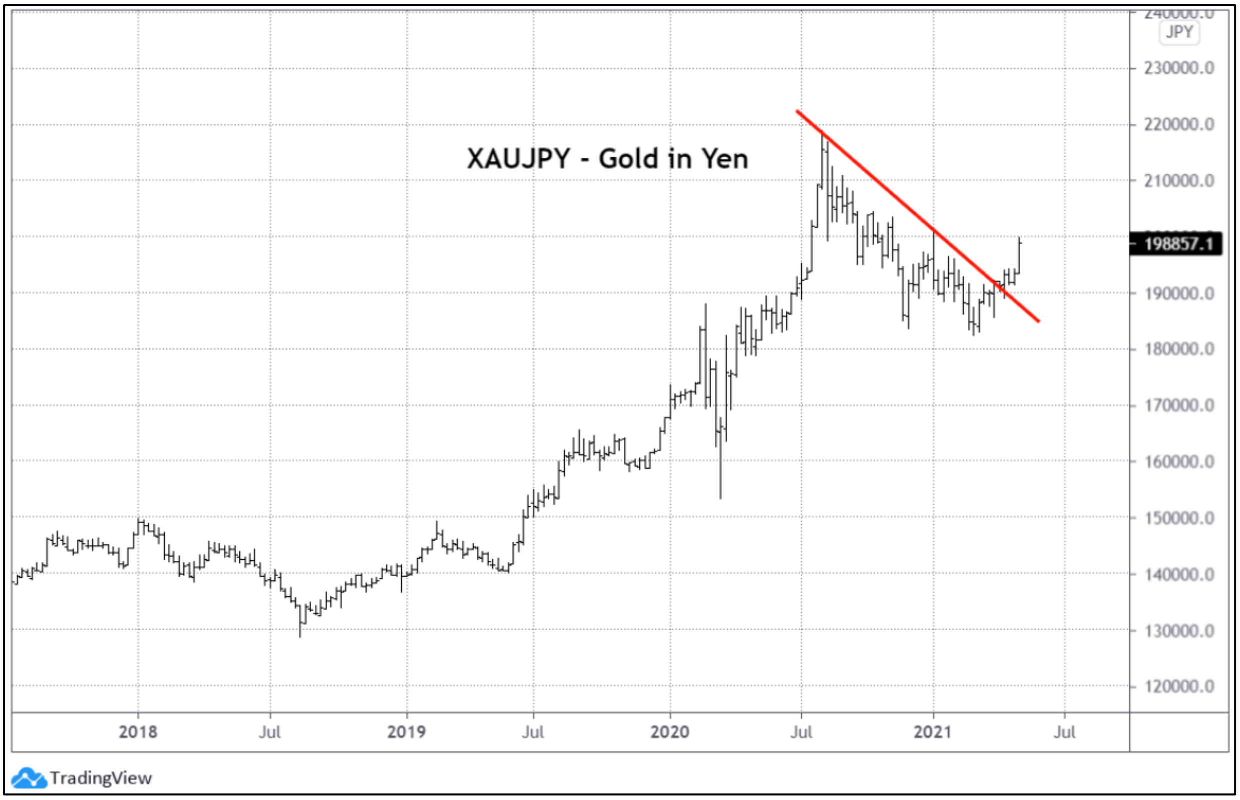


The recent break lower in the USD if maintained will be a big tailwind for Gold as well.

There are other signs of life… Gold and Miners are outperforming bonds.

Stargazer
Asset Management

Gold is starting to outperform other currencies besides the USD.



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US CPI and PPI and various CB speakers will be the main events for the week.

Important Macro Data Releases and Events for the Week

Monday
5/10/2021

- Consumer Price Index YoY (Apr) Forecast: 1%, Prior: 0.4%
- Producer Price Index YoY (Apr) Forecast: 6.6%, Prior: 4.4%

Tuesday
5/11/2021

- ZEW Survey - Economic Sentiment (May) Forecast: 71, Prior: 70.7
- ZEW Survey - Current Situation (May) Forecast: -42.6, Prior: -48.8
- ZEW Survey- Economic Sentiment (May) Forecast: 71.2, Prior: 66.3
- Fed's Williams SPEECH

Wednesday
5/12/2021

- Harmonized Index of Consumer Prices YoY (Apr) Forecast: 2.1%, Prior: 2.1%
- **US Consumer Price Index in its various forms**
- Fed's Clarida SPEECH

Thursday
5/13/2021

- **US Producer Price Index in its various forms**
- Initial Jobless Claims Forecast: -, Prior: 498k
- Initial Jobless Claims 4-week average Forecast: -, Prior: 560k
- Continuing Jobless Claims -, Prior: 3.69m

Friday
5/14/2021

- ECB Monetary Policy Meeting Accounts
- Retail Sales Control Group (Apr) Forecast: 0.8%, Prior: 6.9%

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Retail Sales MoM (Apr) Forecast: 1%, Prior: 9.7%

Retail Sales ex-Auto MoM (Apr) Forecast: 0.9%, Prior: 8.4%

Michigan Consumer Sentiment Index (May) Forecast: 89.5, Prior: 88.3