What to focus on in Global Macro for the week of April 26th, 2021

Macro Themes on the Radar:

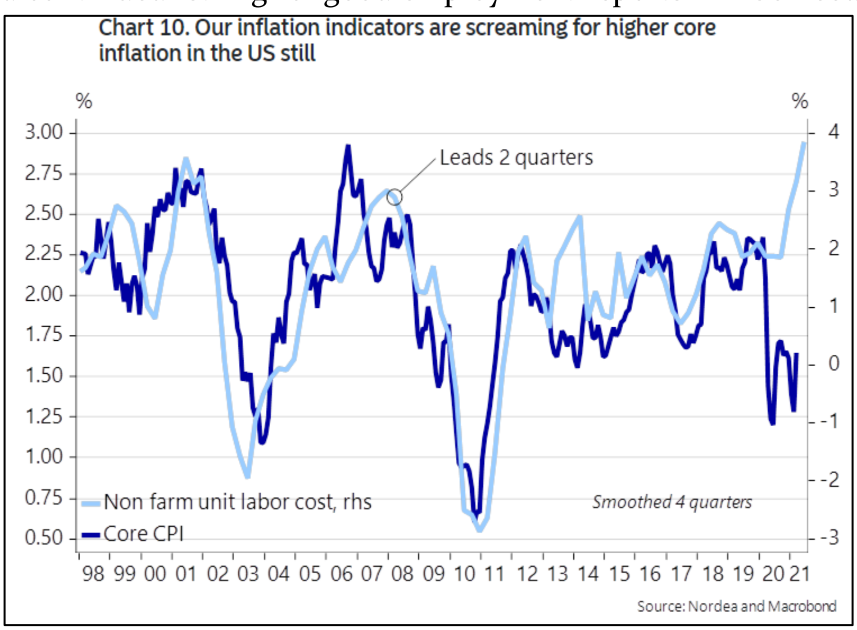
ECB

The ECB meeting came and went on Thursday with nothing new, as expected. Basically, they punted any decisions on tweaking the current rate of net asset purchases until June. I continue to think a few points are worth keeping in mind regarding ECB policy.

- They have expressly said that yields can rise as long as they don't outpace actual economic progress. Yields can go up, but slowly.
- As such, spread control is a primary focus, as big jumps in say Italian vs. German yields would be seen as very disruptive.
- If we head back towards 1.2500 in EURUSD, expect them to restart a round of verbal protests. Although, they don't have a lot of options with which to actively weaken the currency.

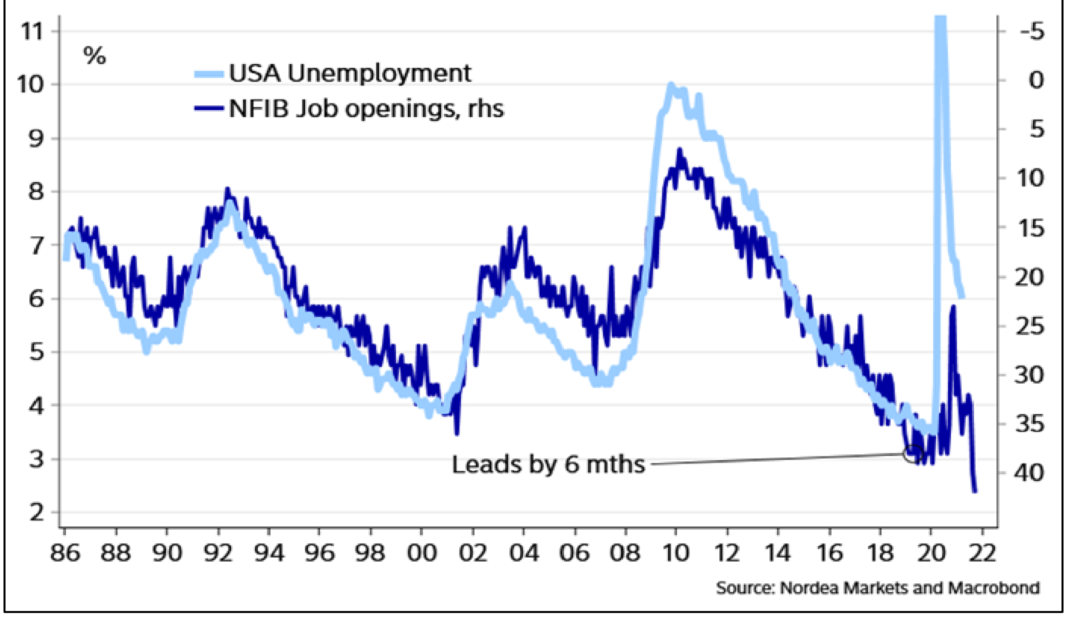
Fed

This week's Fed meeting should largely serve as a check-in on the economic recovery vs. upgraded expectations. Expect a continuing shift towards a more positive tone as we hit Powell's "inflection point" in the economy. With the inflation debate running in high gear for the markets, expect him to continue stressing that the near-term jump in inflation will be transitory and that a continued "string" of good employment reports will be needed before serious consideration is given to policy modifications. Outcomes vs. outlooks will remain the driver now at the Fed. Inflation should continue to push higher and the big debate is around stickiness. We will have to wait and see how that is resolved. Rather than inflation, it could be that sudden and dramatic employment gains over the coming months make it hard for the Fed to justify the current level of accommodation, especially regarding QE.



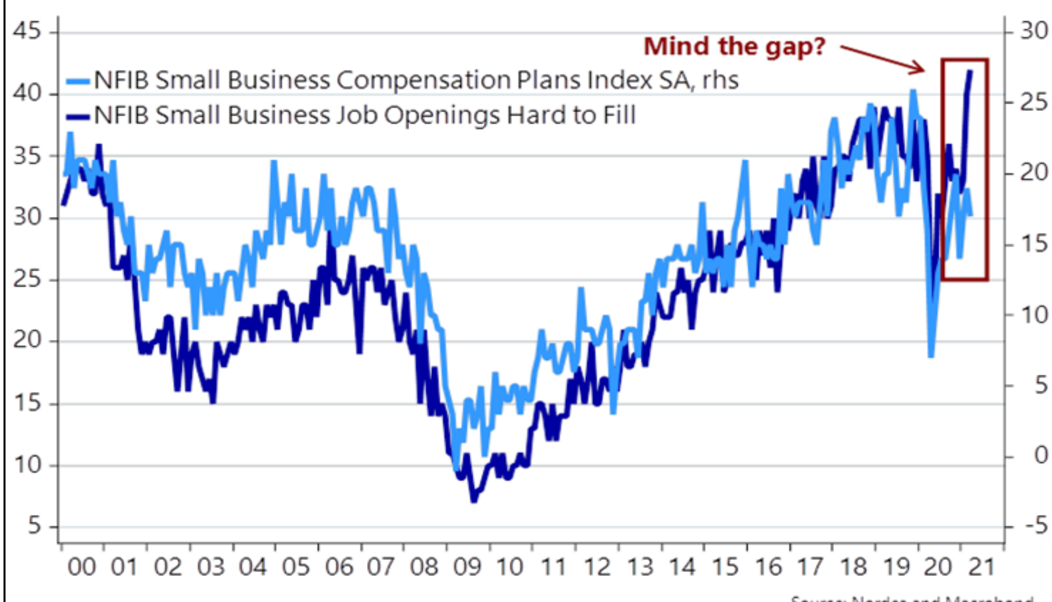
There is plenty of anecdotal evidence that businesses are having a very hard time bringing back people. This could change quickly as restrictions are now easing across the country and people are tired of staying home, despite some continued incentives to do so.

Chart 9. Record low unemployment on the cards in the US much earlier than most people anticipate?



Compensation has been rising but that pressure could slow as people return to work.

Chart 4. Brace yourself – inflation outlook is getting increasingly sticky!



BoJ

This week we also have the Bank of Japan's policy meeting. No new measures are expected, but we will see new growth and inflation projections and it will be interesting to see if any nod is made to the recent resurgence of COVID. Amazingly, Japan has only managed to vaccinate just over 1% of its population so far, lagging far behind most nations.

PMI's

Friday's flash PMI's were again very good globally and in the US.

Commenting on the US PMI data, Chris Williamson, Chief Business Economist at IHS Markit, said:

"The US economy is enjoying a strong start to the second quarter, firing on all cylinders as loosening virus restrictions, an impressive vaccine roll-out, a brighter outlook and stimulus measures all helped boost demand.

The upturn is broad-based: the service sector is growing at the fastest rate recorded in almost 12 years of survey history, and manufacturers reported one of the strongest expansions seen over the past seven years. The latter was all the more impressive, as factories continued to be throttled by unprecedented supply chain delays, a consequence of which was a further steep rise in prices.

The worsening supply situation is a concern for the outlook, especially in relation to prices. Supply needs to improve to come into line with demand. But with record supply chain delays driving a rise in backlogs of uncompleted work of a magnitude not surpassed for over seven years, firms appear to be struggling to boost operating capacity in the near-term."

Good data should continue for the next few months. The numbers will look especially good on a YOY basis given the lockdowns we are measuring against. Higher PMI's tend to be good for equities. However, soon the good PMI's will top out and transition into better employment and inflation numbers, and that is when things get more complicated given the potential policy implications. Last week the Bank of Canada was the first central bank to announce they were going to taper asset purchases. Granted, they have been outperforming the US on the employment front, however, they are likely just the first that will do so.

Risks

Three risks remain at the top of the list for investors.

Inflation, Taxes, and COVID.

As noted above, the inflation debate is raging. Watch the dollar and bond yields for an indication of how people are voting with their investments.

Taxes came to the forefront this week with the announcement that the Administration is mulling a large capital gains tax hike. If the current proposal is passed it would take the top marginal tax rate on investments to 43.4%, one of the highest in the world. It is far from certain that this will be the final proposal or the eventual outcome after Congressional horse-trading.

I have seen a number of pieces on what a capital gains hike has meant for stocks historically. Overall, there has not been much medium-term correlation between equity investments and capital gains taxes. In the short-term, there could however be some downside. Especially given the big gains. I thought these two charts on the subject were interesting.

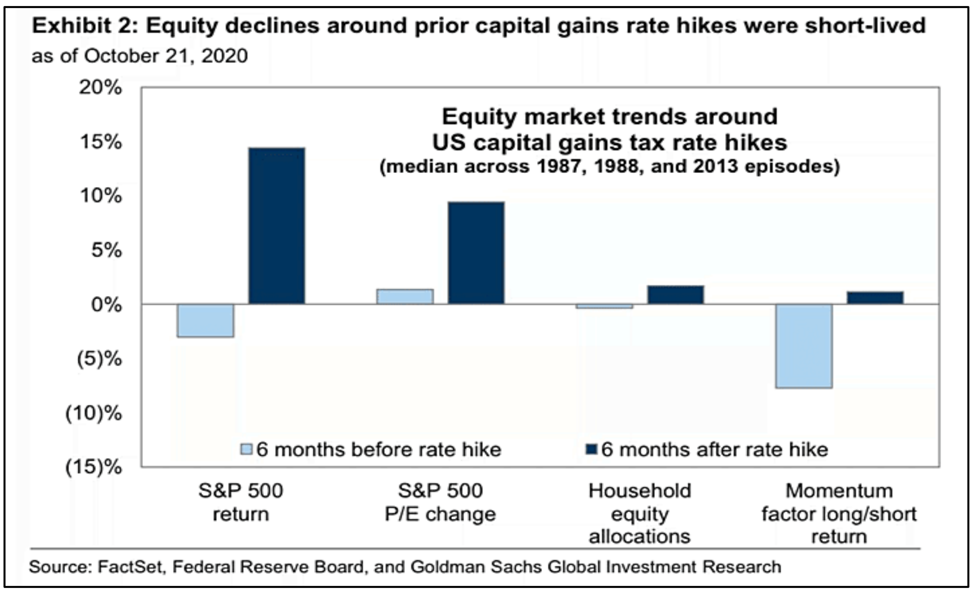
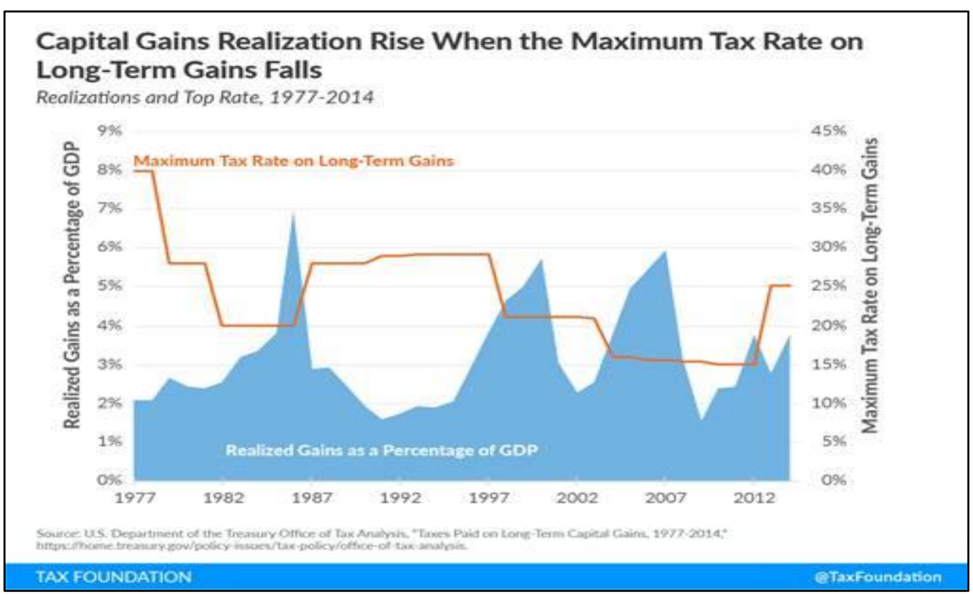


Exhibit 2: Equity declines around prior capital gains rate hikes were short-lived
as of October 21, 2020

Source: FactSet, Federal Reserve Board, and Goldman Sachs Global Investment Research

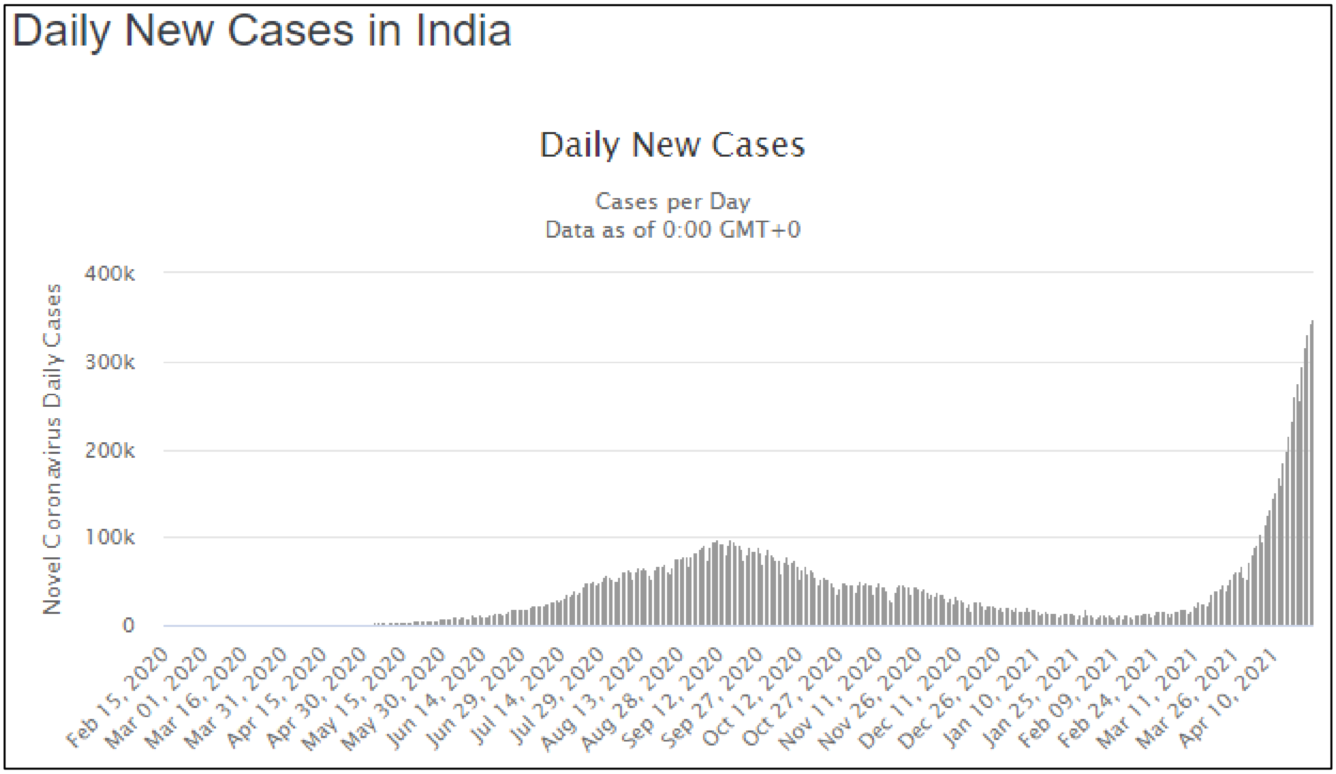


Capital Gains Realization Rise When the Maximum Tax Rate on Long-Term Gains Falls
Realizations and Top Rate, 1977-2014

Source: U.S. Department of the Treasury Office of Tax Analysis, "Taxes Paid on Long-Term Capital Gains, 1977-2014," https://home.treasury.gov/policy-issues/tax-policy/office-of-tax-analysis.

COVID continues to give markets something to think about, given the rate of new cases globally. Multiple economies are facing the threat of fresh restrictions.

India made the news last week as cases soared.



Beyond the obvious tragedy on the ground, investors are worried about what this could mean for global growth. The more global cases there are, the higher the odds that a more dangerous or vaccine-resistant strain emerges. With 1.35Bln people, India provides a lot of opportunity for such a mutation.

<u>What to Focus on Now:</u>

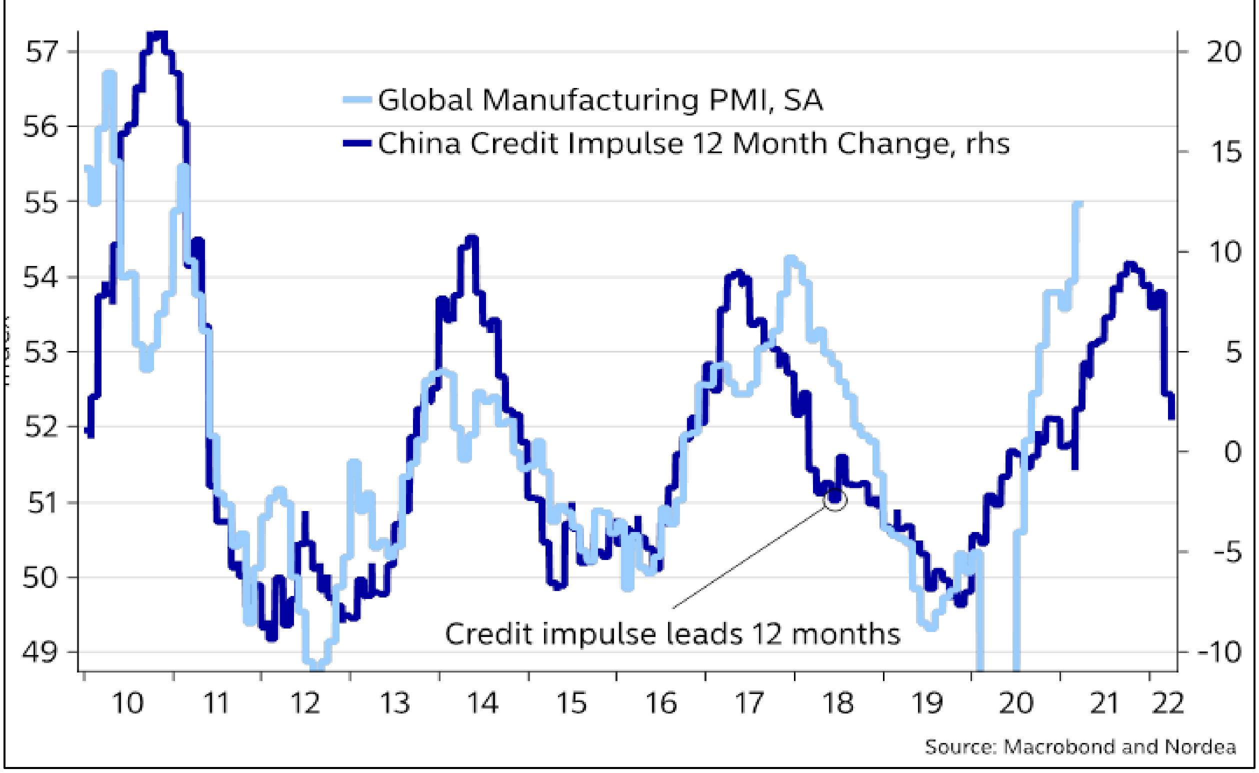
Equities

Lots and lots of noise in equities. Rotation remains violent and the prospect of higher taxes and more COVID cases bounced stocks around last week.

I can't really see why the price action should calm down from here. If anything, volatility should build.

Q2 should still have plenty of positive data prints. However, as we approach Q3 and get the base effects behind us, prints may become more mixed, just as Fed policy-makers start to ponder asset purchases. China/US policy divergence is increasingly interesting.

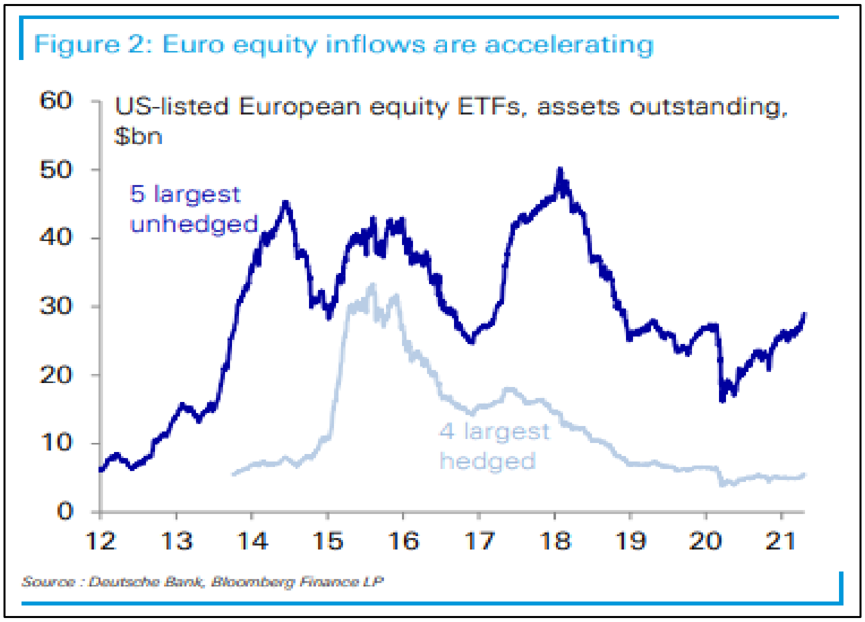
Chart 7. Chinas credit impulse has now clearly rolled over, which doesn't bode too well for H2-2021



Europe

Markets are starting to focus on the upcoming German elections in September. With Merkel heading for the exit, the new CDU/CSU candidate will be Armin Laschet. What has the market particularly interested, is the possibility of the Green party taking the chancellorship. While that doesn't seem the likely outcome at this point, the Greens have pulled ahead in a couple of polls. At a minimum, increased popularity and power for the Greens could push Germany to further embrace European integration and support increased spending on climate friendly projects, and more broadly. Looser purse strings and greater fiscal spending actually supported by Germany, would be a role reversal, and potential game changer. We have a long way to go to get to that point, but this is worth keeping an eye on.

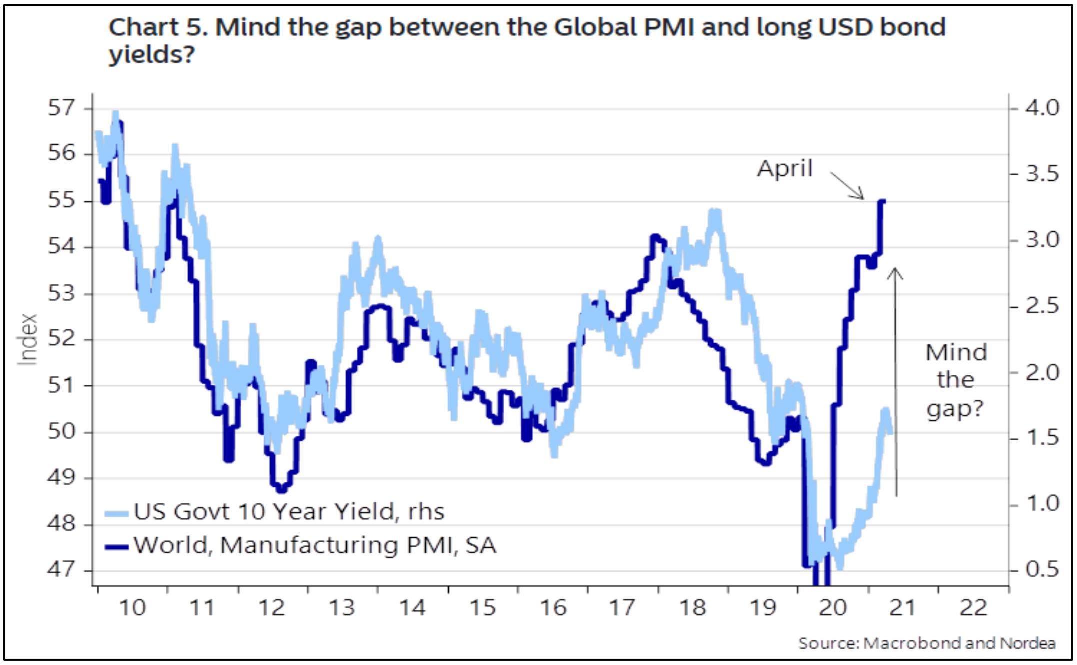
After a long absence, US equity investors are starting to buy European stocks and the EUR.



Bonds

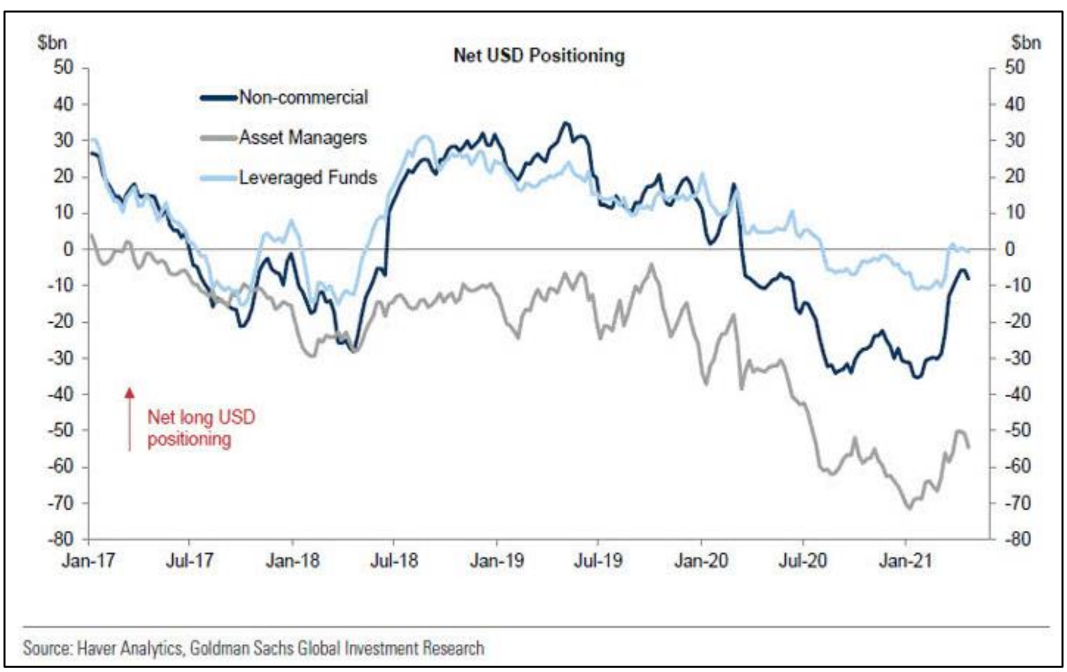
After being extremely oversold, bonds have taken a breather over the last few weeks. It isn't clear that we are done with that retracement yet or what the next catalyst will be to generate another leg down in bond prices. However, they are not nearly as oversold as they were…

The next two months should bring continued very strong data. Do we get another run as the market questions the Fed's ability to keep the taps wide open? Watch claims and employment.

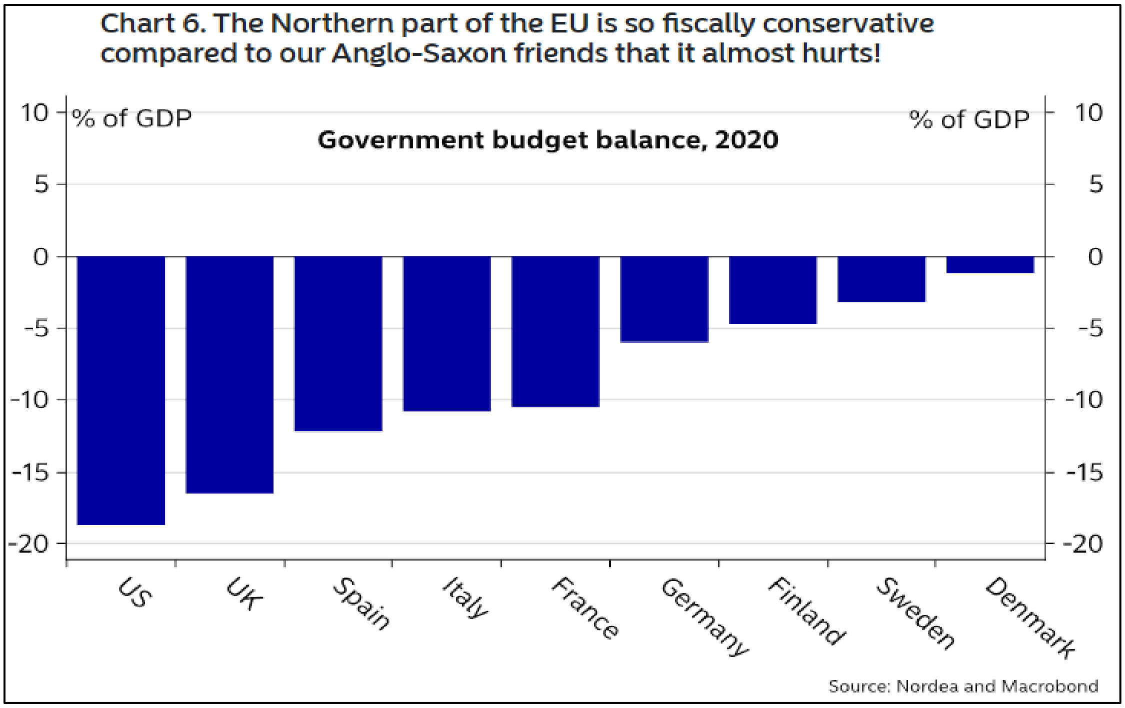


FX - The big back and forth in FX boils down to USD supply vs. the potential growth that it generates domestically. If the US is the leader and the rest of the world follows half-heartedly with continuing COVID concerns and lower levels of fiscal stimulus, the dollar benefits. If, however, the recovery is more synchronized it is likely very bearish for the dollar.

Short USD bets have been greatly reduced.



You can see how the potential for an easier fiscal policy in Germany could get investors excited.



Commodities – Big potential breaks in the ETF commodity plays.

Copper and lumber have been in the news, as have things like corn, wheat and soybeans on the agricultural side. These investments all go to the heart of the inflation and the USD argument.

Watching the prices of bonds and the dollar should provide good information on what the market is pricing going forward. The dollar in particular will make or break the longer-term commodities trade.

Bitcoin

BTCUSD has witnessed a loss of momentum over the last two weeks while some of the other let's say less grounded coins have gone on a wild ride. DOGE is old hat at this point, but there are plenty of other big vol names with amazing market caps whizzing around. Some of the names are great, like Pancake Bunny (200mill market cap) and Rocket Moon, and a few others with names I don't care to put in writing.

I have come to appreciate the potential for blockchain and some of the DeFi applications, but really some of this stuff is hitting new heights of silliness.

For me, it is potentially an interesting window into where we are with regard to risk-taking. In a lot of ways, it's not so different from the price action of the internet companies into the 2000 high. Not many will survive, but the few that do could rule the space.

In any case, it is another way to monitor risk on/off, however with the additional ever-present potential for government intervention. This week's cap gains tax talk didn't help.

Momentum has rolled… in the past, that has ushered in lower or sideways price action for a period.

This week we have the Fed and the BoJ. Biden with give his first speech to a joint session of Congress. We also have initial GDP for Q1 in US and EU.

Important Macro Data Releases and Events for the Week

Monday
4/26/2021

- IFO - Business Climate (Apr) Forecast: 97.7, Prior: 96.6
- IFO - Current Assessment (Apr) Forecast: 94.5, Prior: 93
- IFO - Expectations (Apr) Forecast: 101.4, Prior: 100.4

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	ECB's Panetta SPEECH
	Durable Goods Orders (Mar) Forecast: 2.5%, Prior: -1.2%
	Durable Goods Orders ex-Trans (Mar) Forecast: 1.6%, Prior: -0.9%
	Durable Goods Orders ex- Defense (Mar) Forecast: -%, Prior: -0.8%
	Non-defense Capital Goods Orders ex-Aircraft (Mar) Forecast: -%, Prior: -0.9%
	ECB's Lane SPEECH
	BoJ Interest Rate Decision, Monetary Policy Statement and Press Conf.
Tuesday 4/27/2021	Housing Price Index MoM (Feb) Forcast: -, Prior: 1%
	S&P/Case Shiller Home Price Indices YoY (Feb) Forecast: 11.8%, Prior: 11.1%
	Consumer Confidence (Apr)
	BoC's Maclem SPEECH
Wednesday 4/28/2021	Gfk Consumer Confidence Survey (May) Forcast: -5. Prior: -6.2
	OPEC Meeting
	ECB's President Lagarde SPEECH
	Fed Interest Rate Decision, Monetary Policy Statement and Press Conf.
Thursday 4/29/2021	ECB's De Guinos SPEECH
	Economic Bulletin
	Consumer Confidence (Apr)
	German Buba President Weidmann SPEECH

- Harmonized Index of Consumer Prices YoY (Apr) Forecast: 2%, Prior: 2%
- Initial Jobless Claims Forecast: -, Prior: 560k
- Initial Jobless Claims 4-week average Forecast: -, Prior: -
- Continuing Jobless Claims -, Prior: 3.674
- GDP Annualized Q1 Forecast: 6.5%, Prior: 4.3%
- GDP Product Price Index Q1 Forecast: -, Prior: 1.9%
- PCE Prices QoQ (Q1) Forecast: -, Prior: 1.5%
- Core PCE QoQ (Q1) Forecast: 2%, Prior: 1.3%
- Fed's Williams SPEECH
- CPI ex- Fresh Food YoY (Apr) Forecast: 0%, Prior: -0.1%
- Non-Manufacturing PMI (Apr) Forecast: 52.6, Prior: 56.3
- NBS Manufacturing PMI (Apr) Forecast: 51.4, Prior: 51.4

Friday
4/30/2021

- GDP Q1 Across Europe
- CPI YoY (Apr) Forecast: 1.6%, Prior: 1.3%
- CPI - Core YoY (Apr) Forecast: 0.9%, Prior: 0.9%
- Core - PCE Price Index YoY (Apr) Forecast: 1.8%, Prior: 1.4%
- Chicago Purchasing Managers Index (Apr) Forecast: 63, Prior: 66.3
- Michigan Consumer Sentiment Index (Apr) Forecast: 88, Prior: 86.5

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