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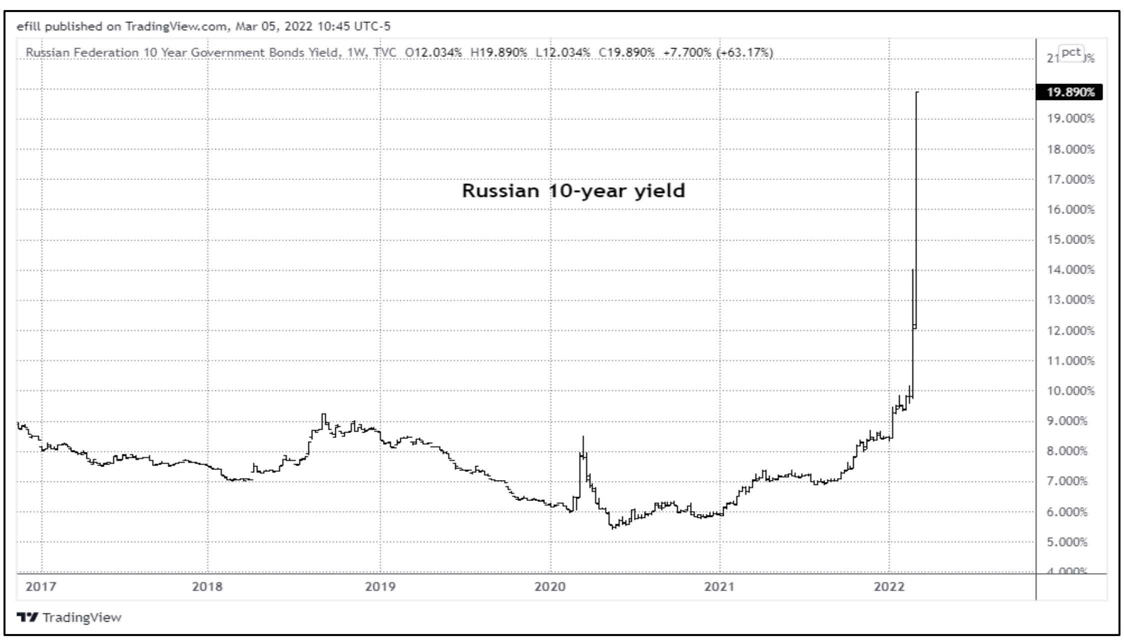
<u>What to focus on in Global Macro for the week of March 7th, 2022</u>

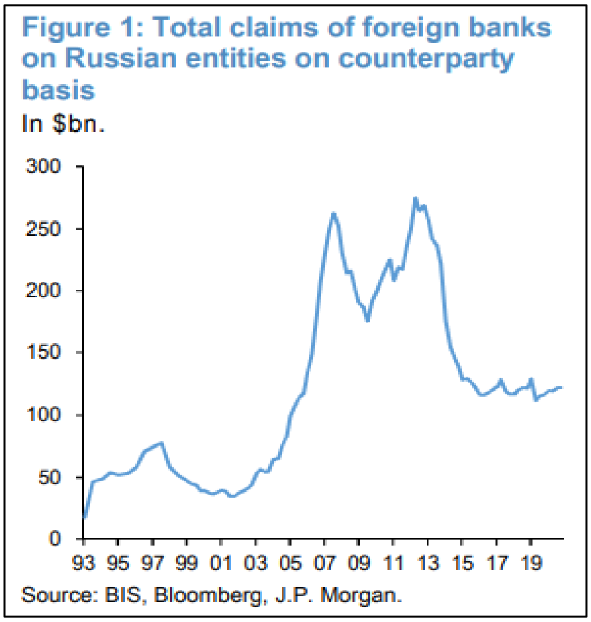
As the war in Ukraine, inflation, and Fed policy expectations continue to dominate all other inputs, Macro considerations are ruling markets. As with COVID and its consequences, the word "unprecedented" can again be applied over and over to the outcomes we are seeing.

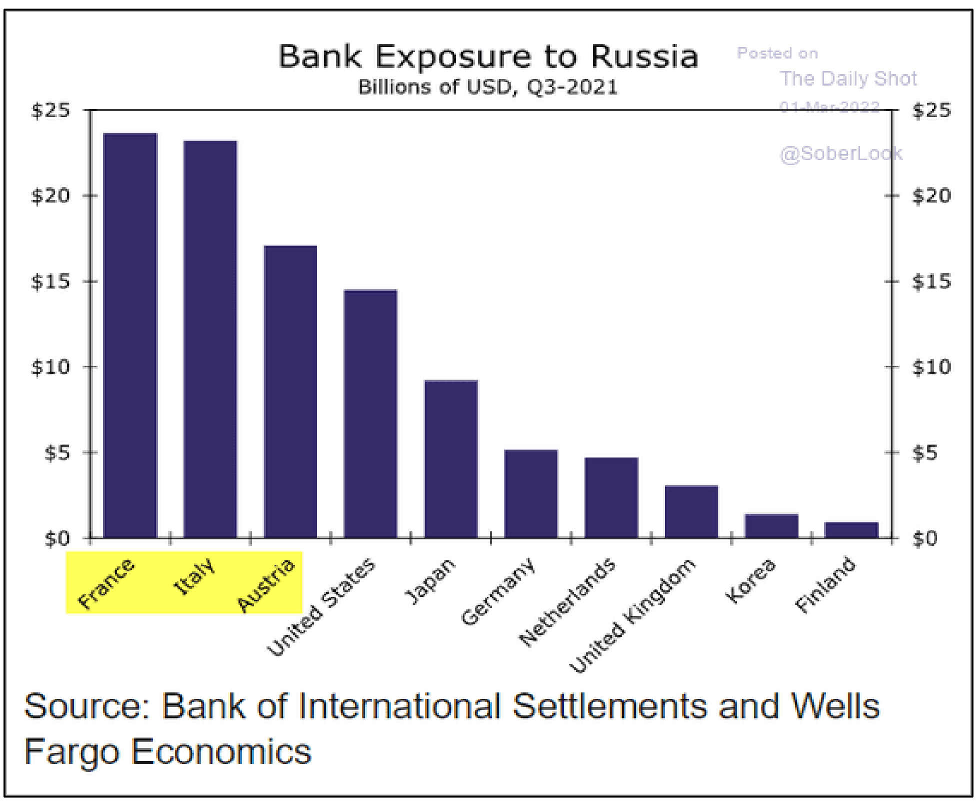
There are dramatic developments unfolding across many different markets. The price action in Russian markets (those that are open) illustrates the reflexive effects of an economy heading for a cliff edge. The Ruble is down 40% as 10-year yields approach 20%.



Direct exposure to Russia is actually relatively low both in terms of ownership of financial assets by US investors, and exposure from Western banks.

It seems the 2013/2014 round of sanctions after Russia's annexation of Crimea had already dissuaded investment and lending. The exposure that does exist is primarily out of Europe.





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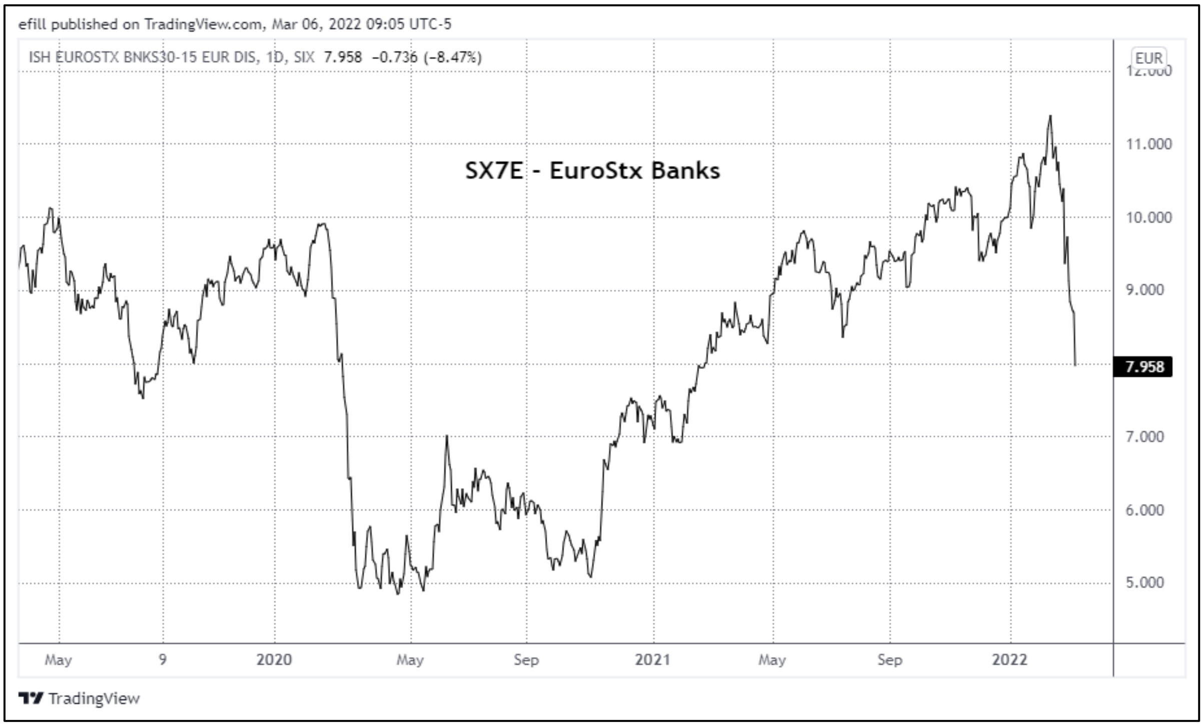
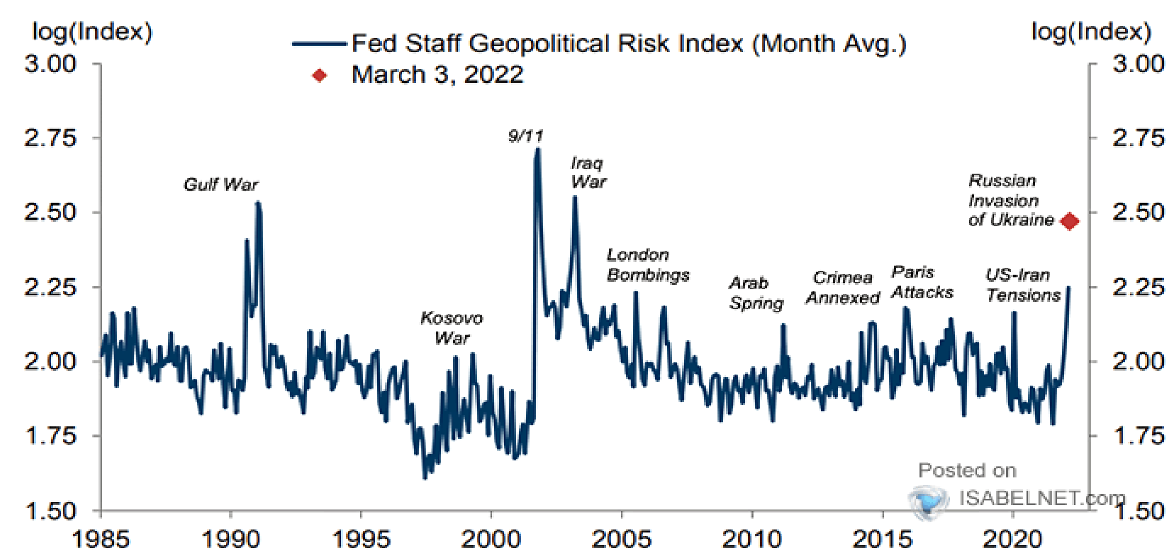
As a result, European banks have been felt the one-two-punch of Russian credit exposure and the fear of damaging effects on the European economy, which has quickly knocked down ECB rate hike expectations. We will see how the ECB frames the situation at this Thursday's meeting.



No doubt, the Fed is eyeing the situation carefully as well. So far, Powell looks undeterred as the March meeting approaches, at least for a few initial hikes.

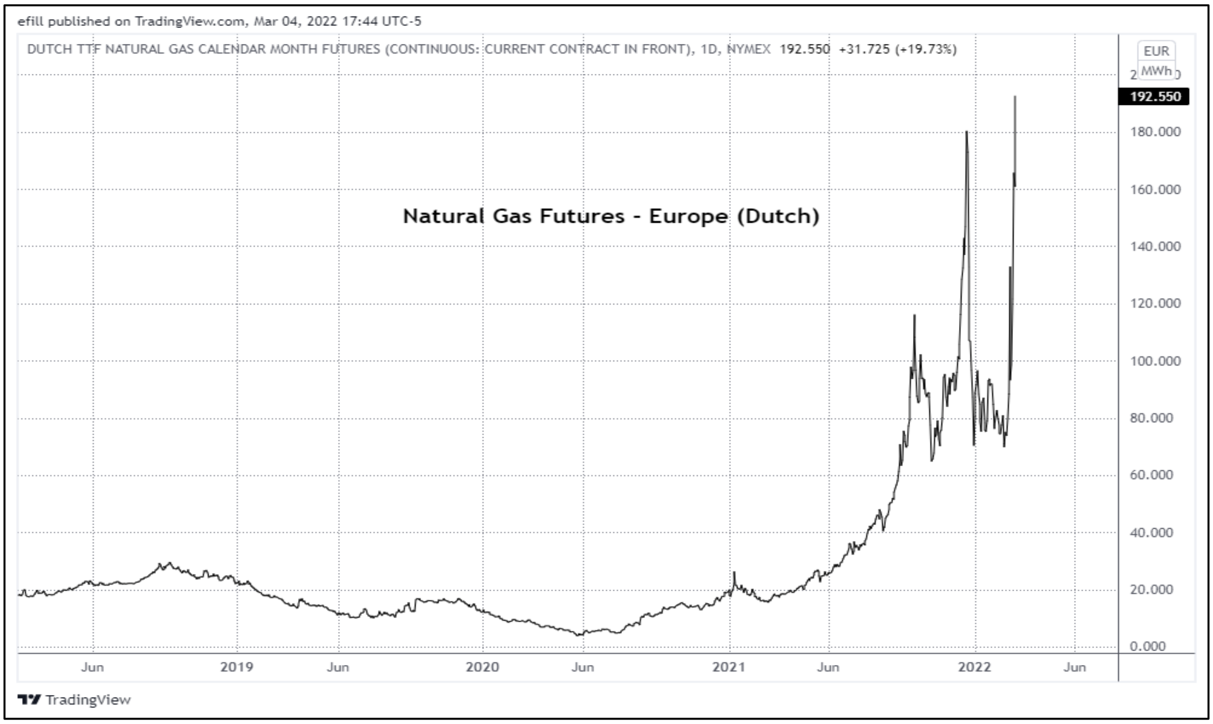
Exhibit 1: Geopolitical Risk Has Risen Sharply Due to the Russia-Ukraine Conflict



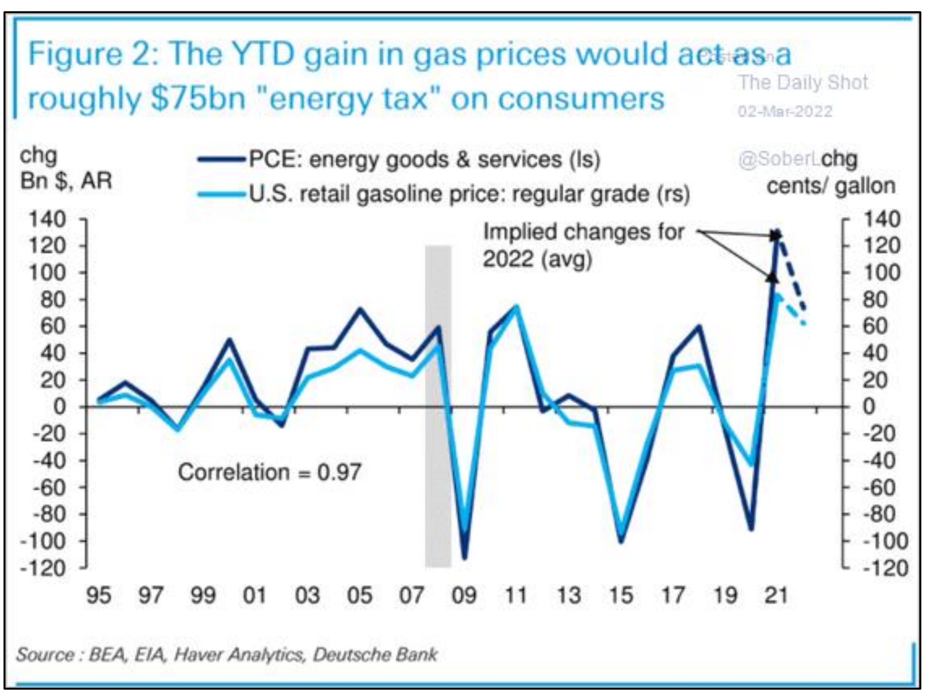
Source: Federal Reserve, Goldman Sachs Global Investment Research

Markets have been reducing some of the hike expectations for later in the year as markets worry that the jump in energy prices is becoming increasingly destructive to economic growth.

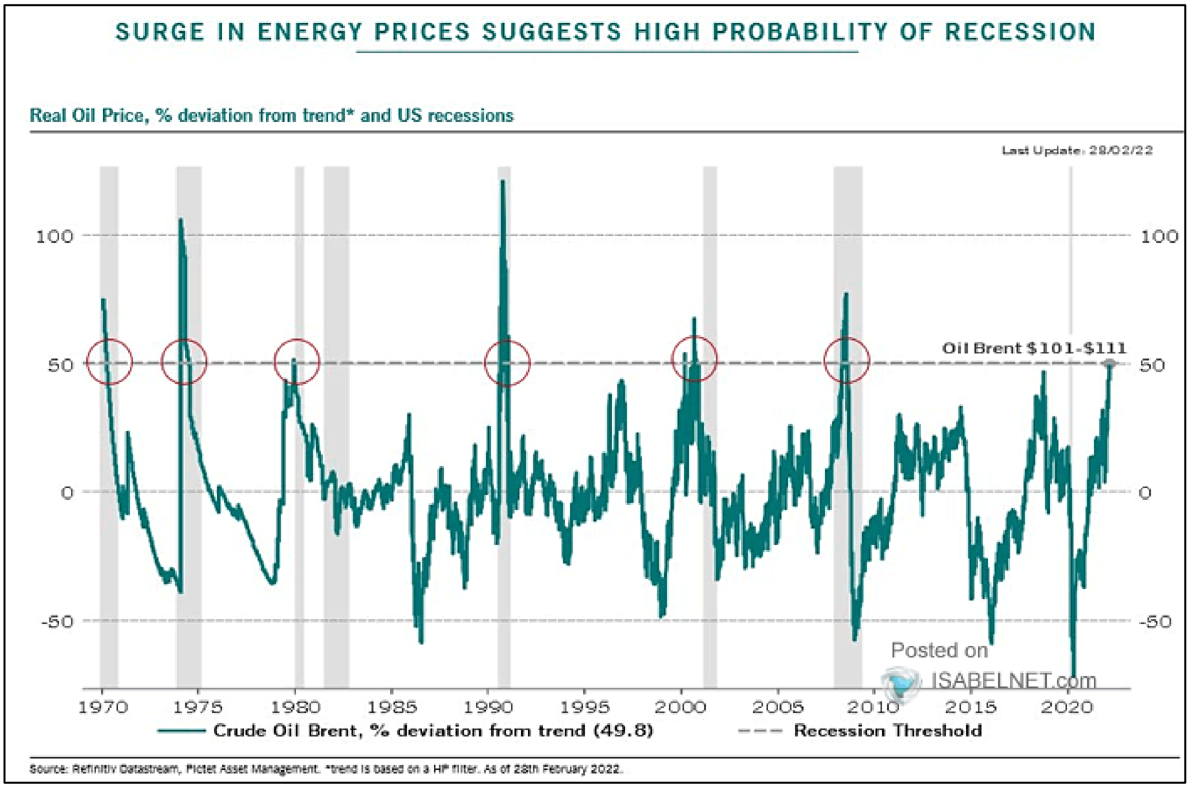
European natural gas has been at the epicenter of the move, but oil and coal prices have exploded as well.



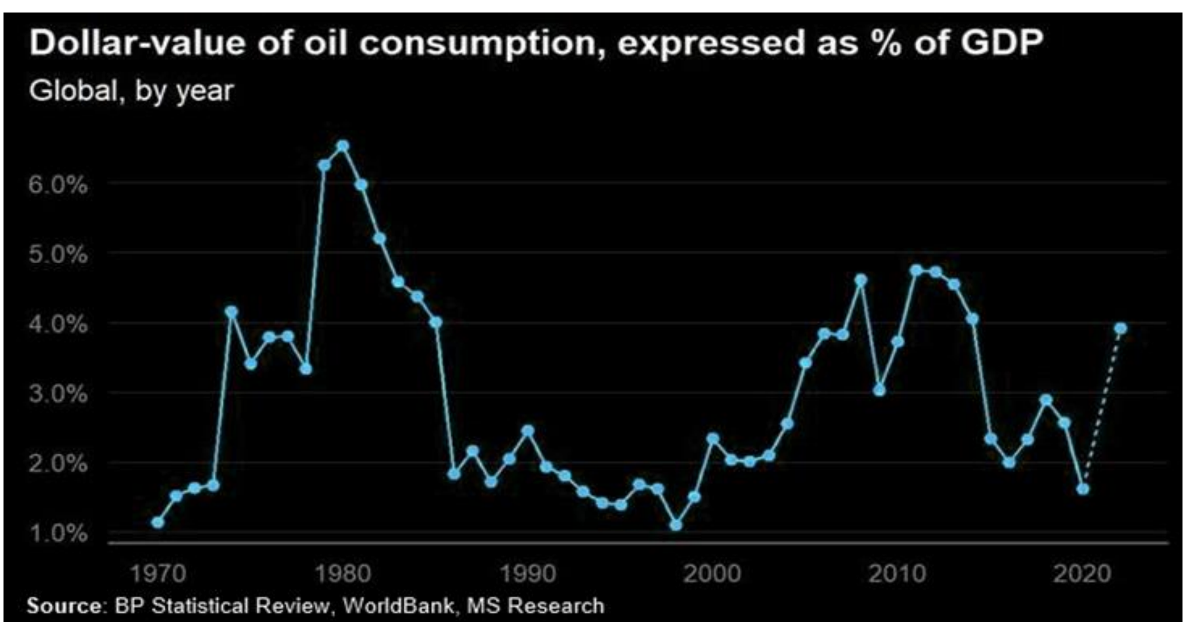
How big a tax on consumers will energy become?



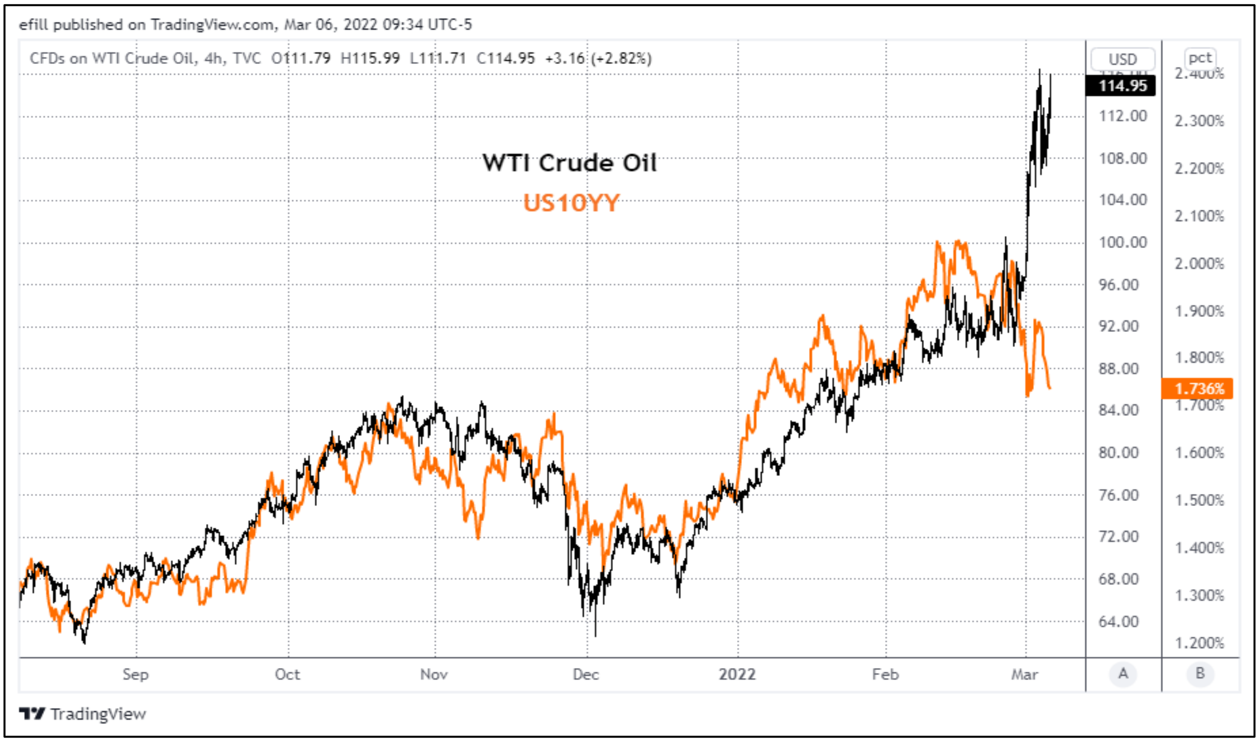
Historically, large runups in energy prices have often preceded recessions. Frequently, because they led to Fed tightening to cool inflation.



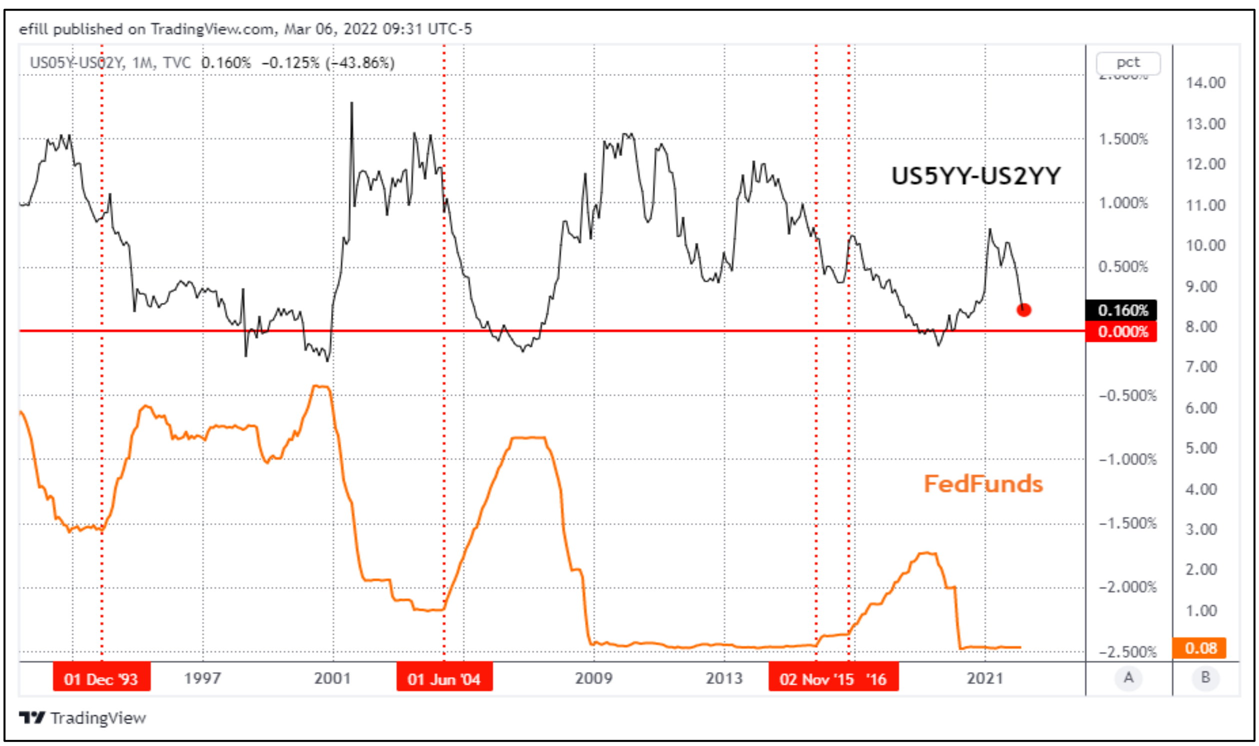
If you look at oil prices adjusted for inflation or disposable personal income they still aren't anywhere near where they were in the late '70's or even 2008. The next chart shows a similar picture. Having said that, the higher the price goes, the greater the danger to the economy.



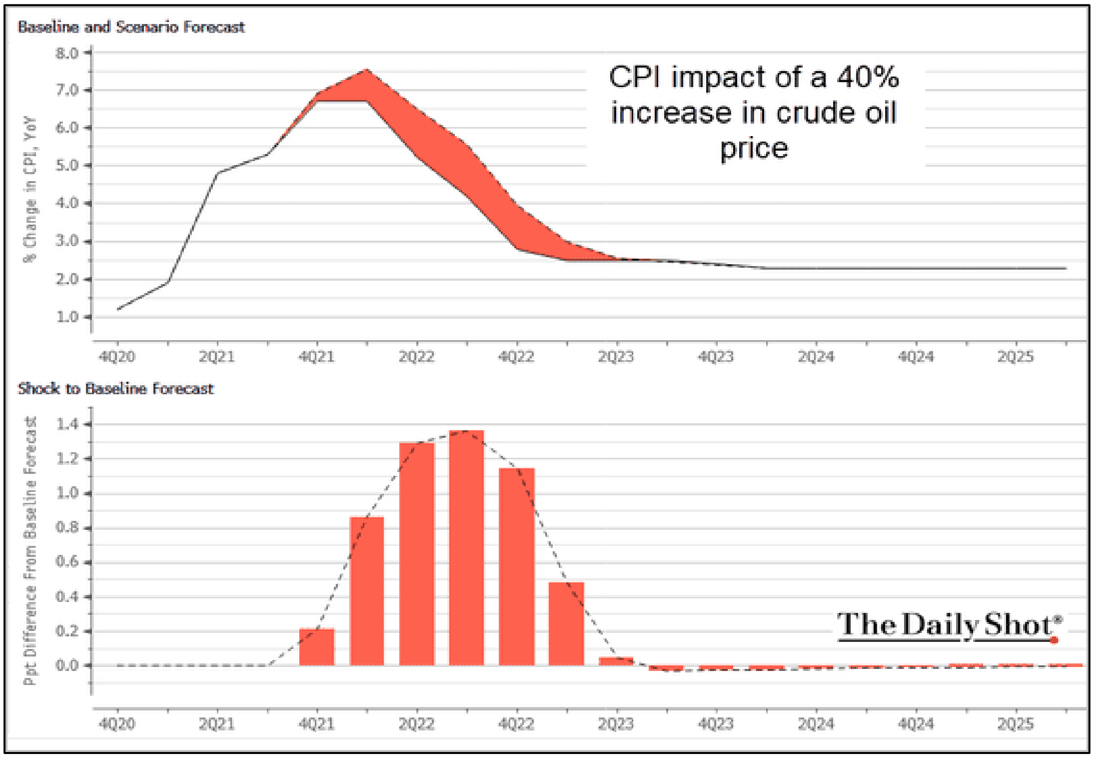
The rolling over of yields likely reflect both safe-haven capital flows and concerns that strong growth and high inflation could turn into a more stagflationary environment.



Various curves continue to flatten, even before Fed hikes start.



The Fed is faced with inflation that will likely be higher for longer, given the most recent move in energy prices.



Having waited too long, the Fed has now painted itself into a corner. The quick succession of demand and supply shocks we have seen now leaves them with the difficult choice of how much to hike into a potentially destructive energy supply shock.

Given the backdrop, US equity indices have held up relatively well.

Europe, which had seen a lot of incoming flows in recent months, has been hit hard as you might expect given its economic and geographic exposure. The overweight positioning going in has undoubtedly not helped the price action.

In mid-February, before the invasion kicked off, my inflection point signal was triggered in Euro Stoxx. The red lines on the chart illustrate those levels over the last couple of years. When triggered, you tend to get move volatility and large directional moves, which can be monetized via the right options structure.

Initially, it held up, but has been hit hard over the last week as the Ukraine crisis deepened.

Given the falling Euro and relative equity market price action, it looks like at least some safe-haven flows into the US are occurring.

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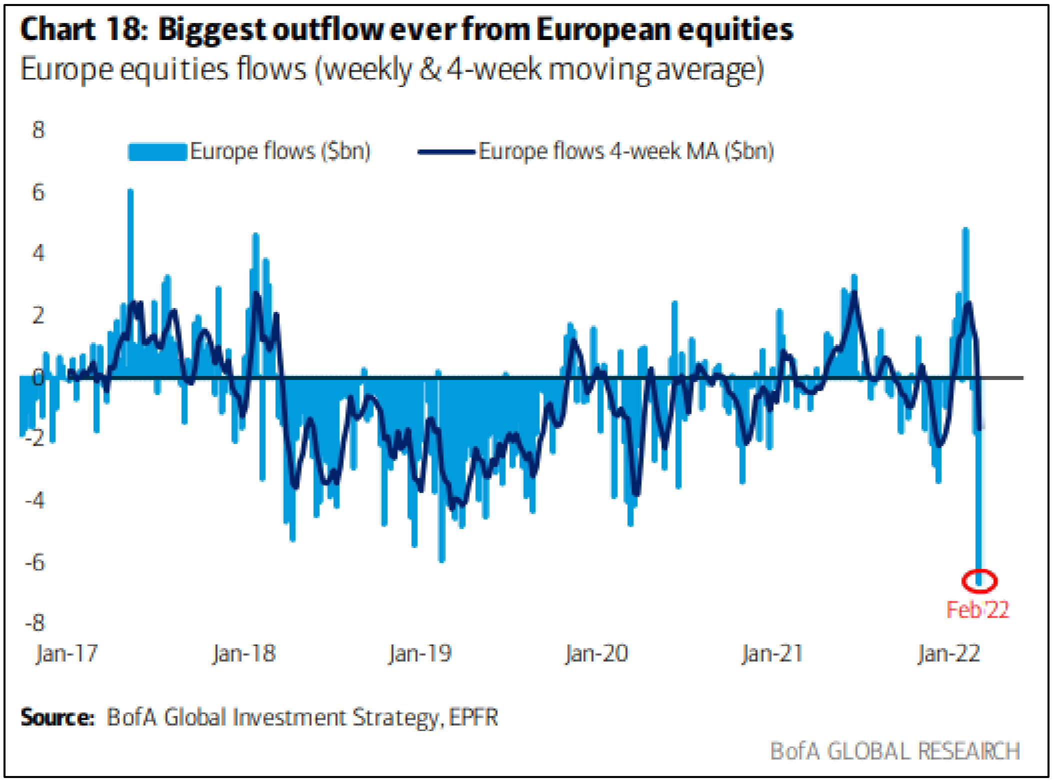

Here are recent and historical inflection point triggers for the SPX and NDX.

Last weeks jump in the dollar was led by a 3% fall in the Euro.

EURUSD now has some very big levels between 1.0900 and 1.0700.

Unsurprisingly, GBP has held up better but is now also facing a big level just below.

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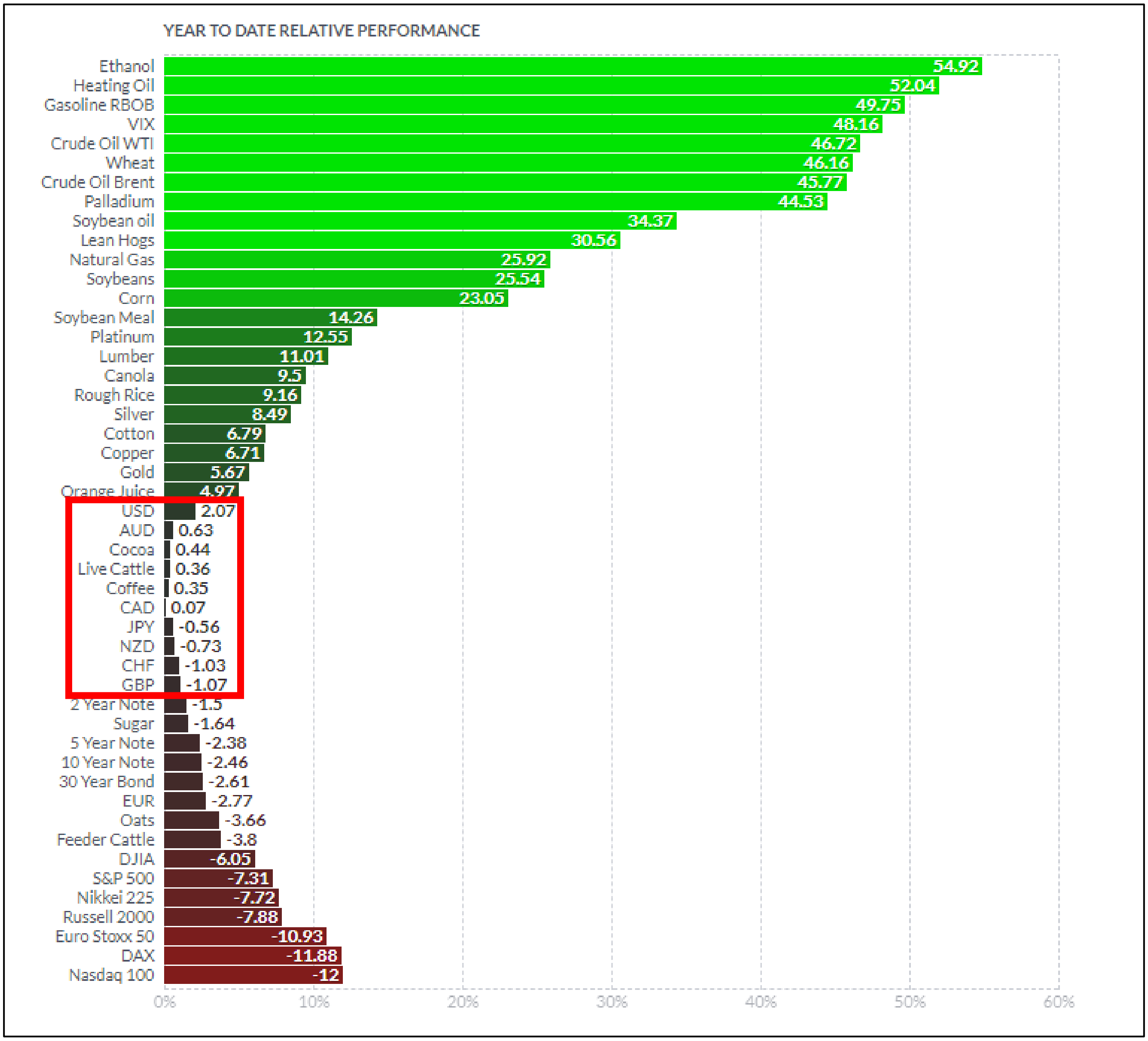
FX has been getting pulled in various directions resulting in a very whippy range over the last few months.

The YTD (as of Thursday) for various asset classes illustrates how stuck it has been.



However, the end-of-week move may have cracked that range now. We will see if FX volatility is now back.

AUDUSD has been particularly interesting as it has broken its usual risk on/off correlations and has been diverging from many of the other dollar pairs.

The poster child for this has been the move in EURAUD.

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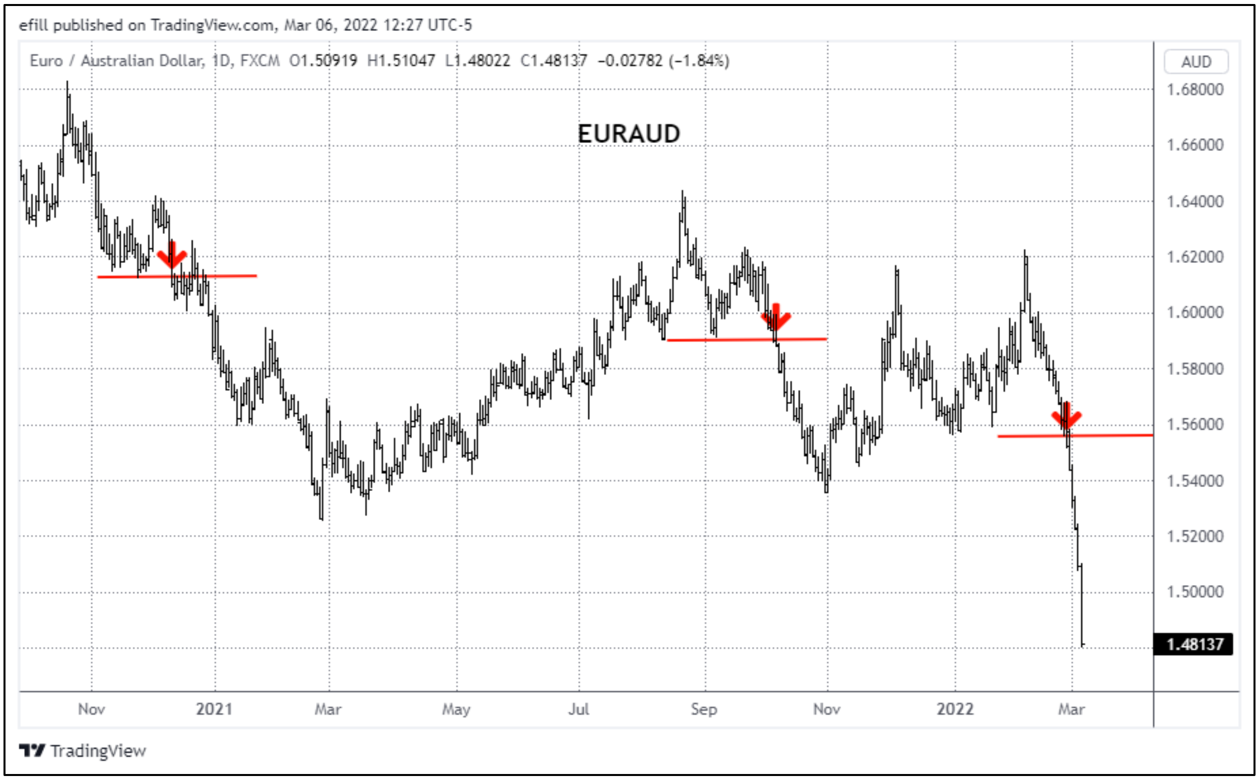
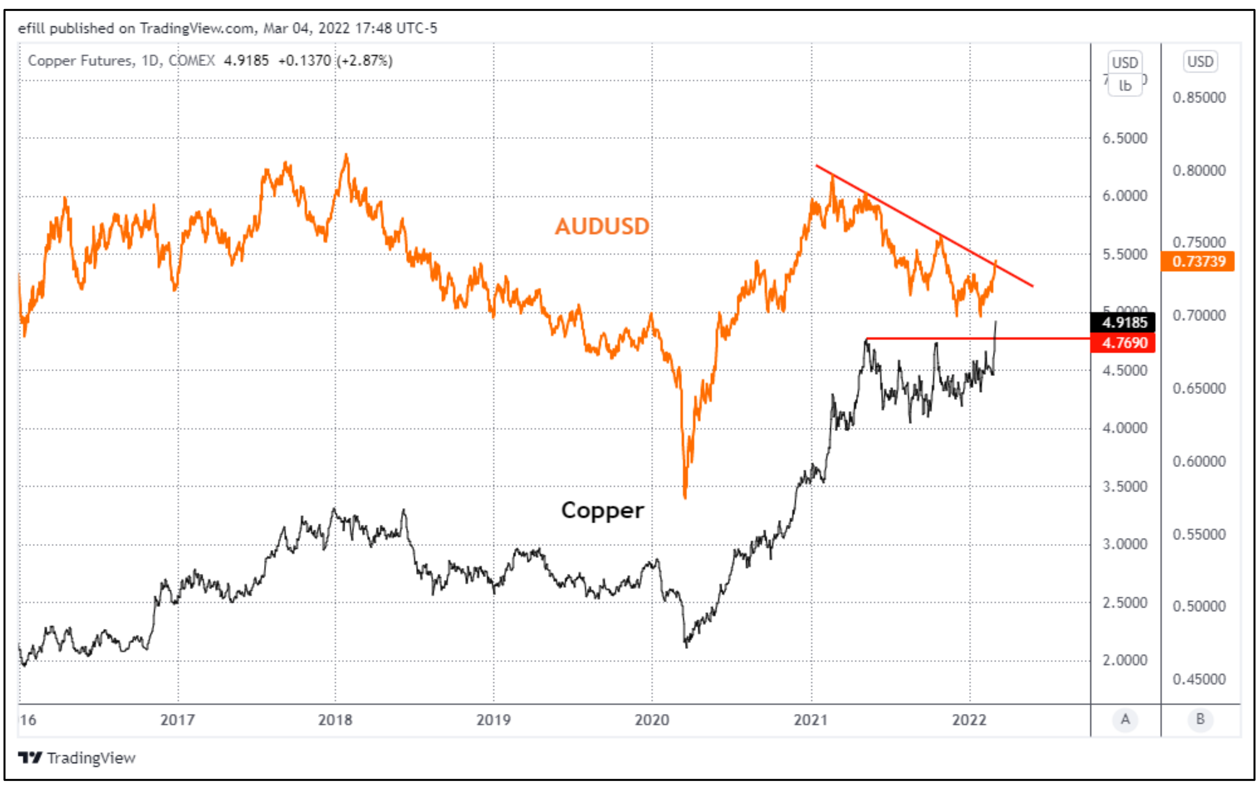
Having broken one of my inflection points the previous week, it fell out of bed last week.



Is the AUD price action reflective of renewed strength in commodities like copper and gold?



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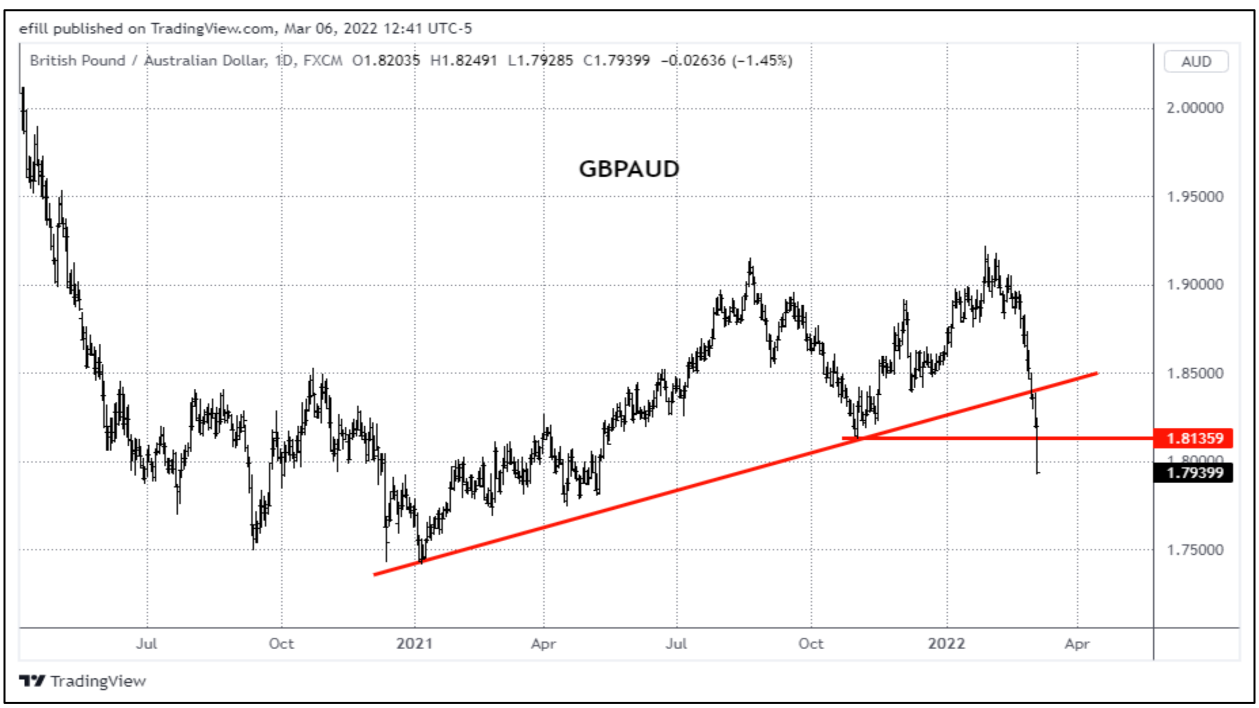
Or are we seeing some flight to safety here too, as foreign investors are reluctant to hold as many EUR or USD given the current geopolitical situation, and Australia represents geographic diversification?

In any case, AUD strength has been broad, and like gold, has broken the dollar link.



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And … that brings us to Gold. Last week, saw a potentially big break higher.

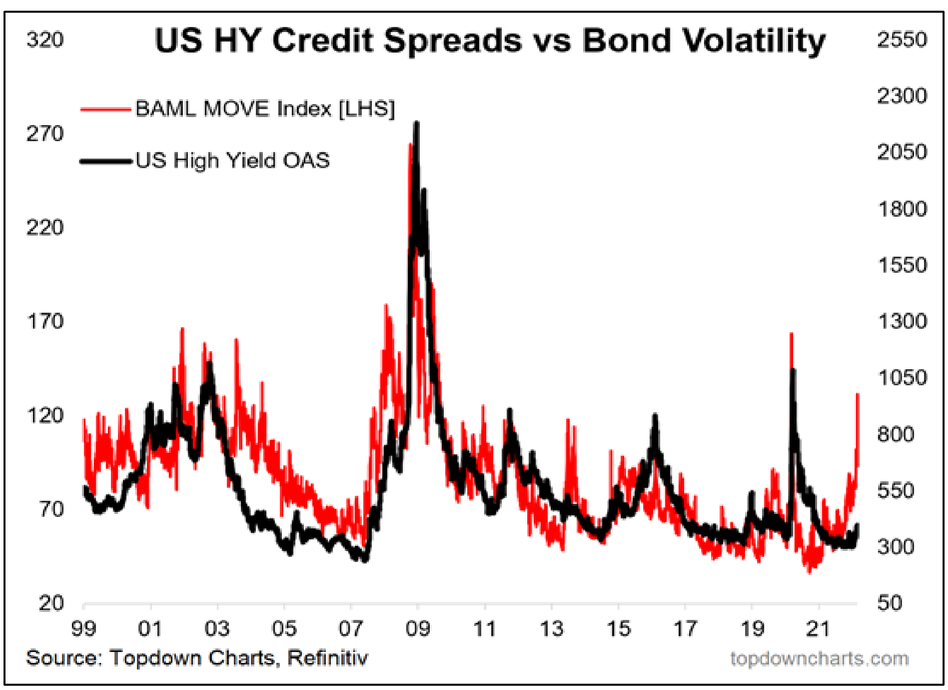
Given the EUR weakness, XAUEUR has been the best trade so far.

This relative move in gold miners is worth watching. Back to the top of the range?

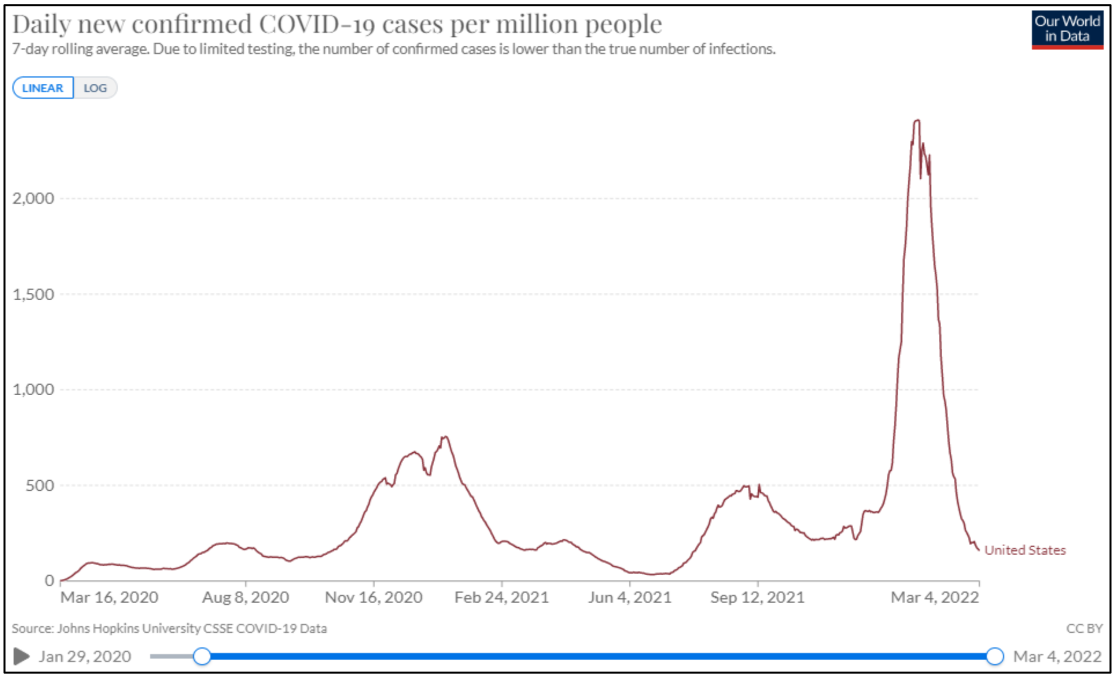
Silver has started to come to life as well and looks particularly interesting vs. EUR.

Finally, a pricing of further concerns about global growth may help Gold here. Over the last decade, Gold has tended to do well when Treasuries hold their own, or even outperform, vs. equities.

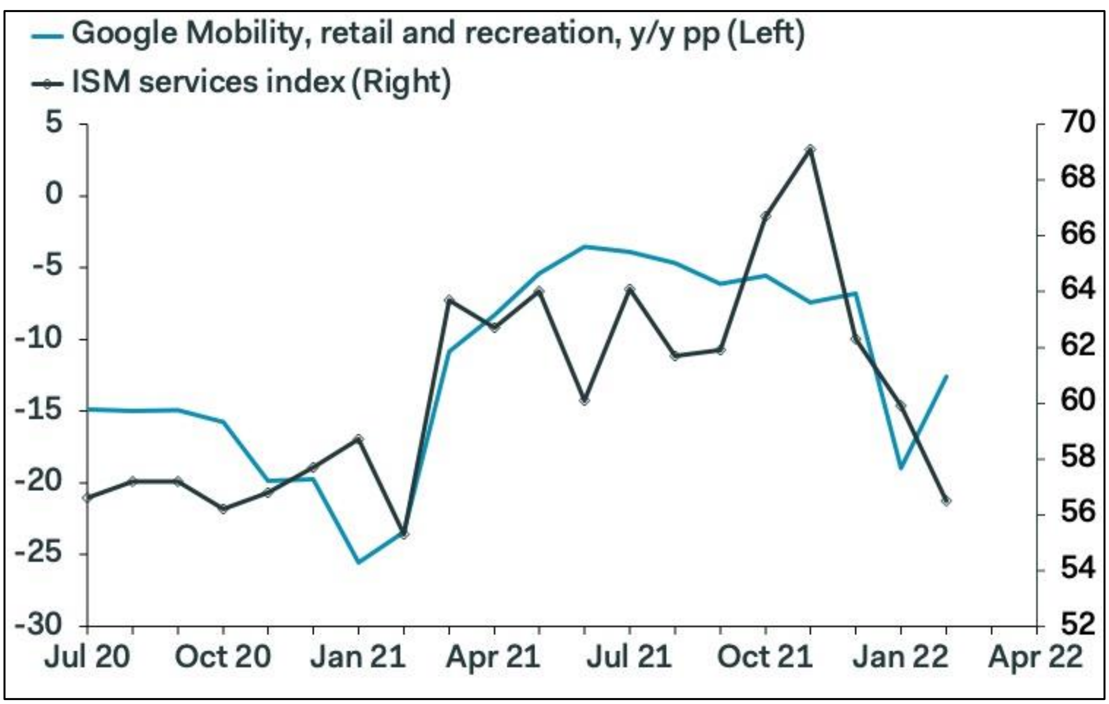
Here are a few additional charts I think are worth noting…



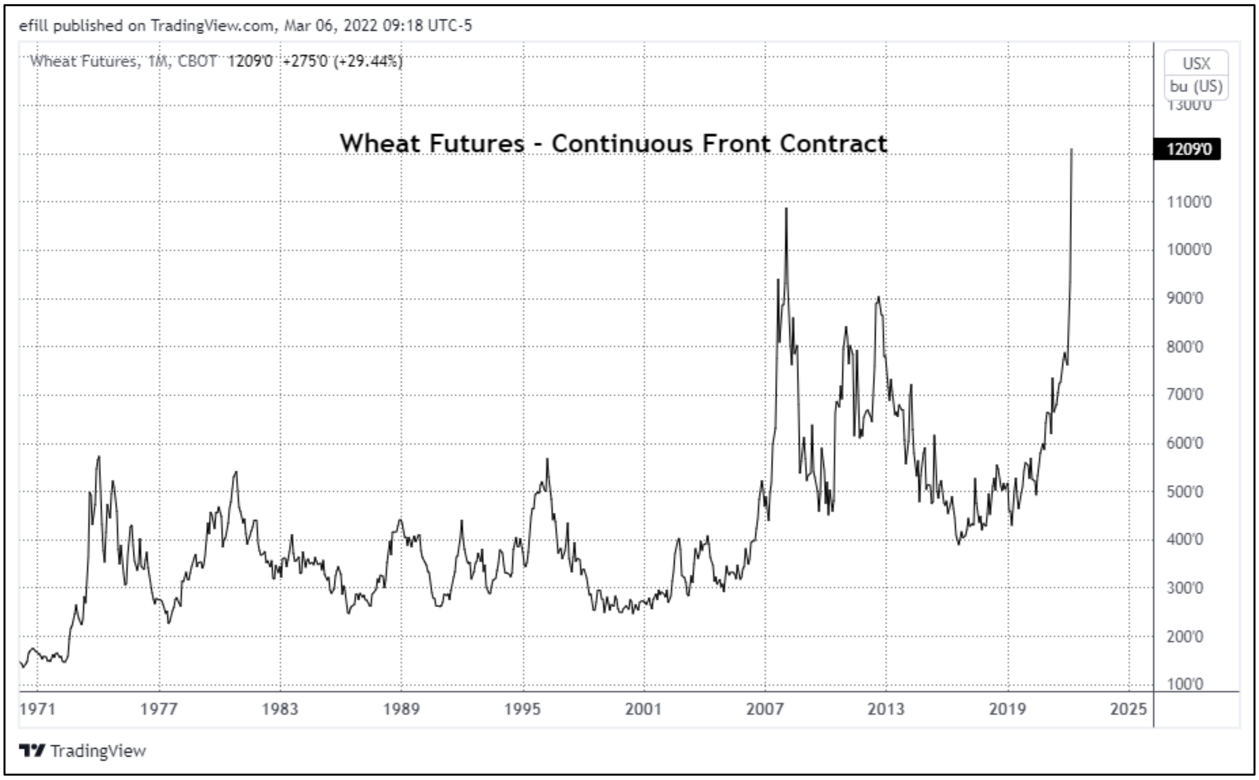
Between the falling US case count and the Ukraine crisis, COVID has all but disappeared from the news cycle.



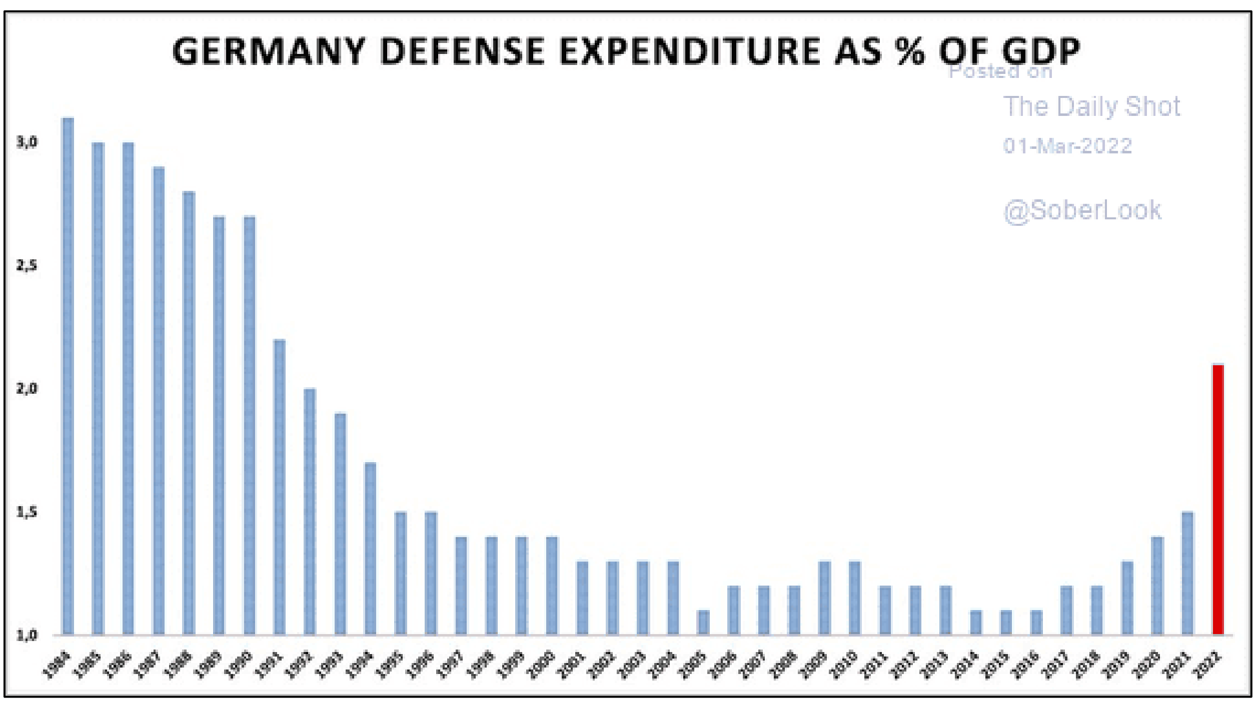
Could a resulting uptick in activity counteract some of the energy price negativity?



Political consequences from the rise in global food prices may be coming. Ukraine and Russia account for 25% of global wheat production.



A big change in Europe regarding defense spending is underway.



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Ukraine, CB policy and inflation data continue to take center stage…

The one thing that could change the entire landscape in an instant would be a Russian coup. Likely? Probably not, but with an imploding economy and daily troop losses now rivaling what they were losing in a year during their Afghanistan adventure, it isn't a zero probability.

Important Macro Data Releases and Events for the Week

Monday 3/7/2022	Factory Orders and Retail Sales (Jan)
Tuesday 3/8/2022	GDP Q4
	CPI (Feb)
Wednesday 3/9/2022	RBA Debelle speech and Consumer Inflation Expectations
Thursday 3/10/2022	**ECB Interest Rate Decision, Policy Statement, and Press Conference**
	CPI (Feb)
	Initial Jobless Claims
	Initial Jobless Claims 4-week average
	Continuing Jobless Claims
Friday 3/11/2022	Harmonized Index of Consumer Prices (Feb)
	Employment Data (Feb)
	Michigan Consumer Sentiment Index (Mar)

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